No. 80-84

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

ANDERSON BROS. FORD and
FORD MOTOR CREDIT COMPANY,

Petitioners,

vs.

OLGA VALENCIA and
MIGUEL GONZALEZ,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF THE PETITIONERS

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QUESTIONS PRESENTED

1. Under the Truth in Lending Act and Regulation Z thereunder, is an assignment of returned or unearned insurance premiums a "security interest" requiring disclosure on the face of an automobile retail installment sales contract?

2. As the prevailing case law and industry-wide commercial usage at the time of execution of the contract form *sub judice* supported *not* disclosing the assignment of returned or unearned insurance premiums as a "security interest", should any ruling to the contrary be made prospective only?

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BRIEF OF THE PETITIONERS

OPINIONS BELOW

The opinion of the Court of Appeals (J.A. 38-64) is reported at 617 F.2d 1278. The opinions of the District Court (J.A. 9-21, 33-35) are not reported.

JURISDICTION

The Judgment of the United States Court of Appeals for the Seventh Circuit was entered on March 20, 1980. The order denying Defendants' timely Petition for Rehearing was entered on April 22, 1980 (J.A. 66). The Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit was timely filed on July 19, 1980. On November 10, 1980, this Court granted the Petition for a Writ of Certiorari limited to questions one and two presented by the Petition.

The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The statute and regulations involved in this case are: Consumer Credit Protection Act, § 128(a)(10), 15 U.S.C. § 1638(a)(10):

> (a) In connection with each consumer credit sale not under an open end credit plan, the creditor shall disclose each of the following items which is applicable:
>
> • • • •
>
> (10) A description of any security interest held or to be retained or acquired by the creditor in connection with the extension of credit, and a clear identification of the property to which the security interest relates.

Regulation Z, 12 C.F.R. § 226.2(gg) (1980):

> "Security interest" and "security" mean any interest in property which secures payment or performance of an obligation. The terms include, but are not limited to, security interests under the Uniform Commercial Code, real property mortgages, deeds of trust, and other consensual or confessed liens whether or not recorded, mechanic's, materialmen's, artisan's, and other similar liens, vendor's liens in both real and personal property, the interest of a seller in a contract for the sale of real property, any lien on property arising by operation of law, and any interest in a lease when used to secure payment or performance of an obligation.

Regulation Z, 12 C.F.R. § 226.8(b)(5) (1980):

> (b) *Disclosures in sale and nonsale credit.* In any transaction subject to this section, the following items, as applicable, shall be disclosed:
>
> • • • •
>
> (5) A description or identification of the type of any security interest held or to be retained or acquired by

the creditor in connection with the extension of credit, and a clear identification of the property to which the security interest relates or, if such property is not identifiable, an explanation of the manner in which the creditor retains or may acquire a security interest in such property which the creditor is unable to identify. In any such case where a clear identification of such property cannot properly be made on the disclosure statement due to the length of such identification, the note, other instrument evidencing the obligation, or separate disclosure statement shall contain reference to a separate pledge agreement, or a financing statement, mortgage, deed of trust, or similar document evidencing the security interest, a copy of which shall be furnished to the customer by the creditor as promptly as practicable. If after-acquired property will be subject to the security interest, or if other or future indebtedness is or may be secured by any such property, this fact shall be clearly set forth in conjunction with the description or identification of the type of security interest held, retained or acquired.

STATEMENT OF THE CASE

On September 30, 1977, Olga Valencia and Miguel Gonzalez (the "Buyers") purchased a used 1974 Ford Pinto from Anderson Bros. Ford pursuant to an Illinois Automobile Retail Installment Contract (the "Contract"), a full-sized copy of which is attached at the end of the Joint Appendix. The Contract was subsequently assigned for value by Anderson Bros. Ford to Ford Motor Credit Company.[1]

As required by the Truth in Lending Act (the "Act"), 15 U.S.C. § 1601 *et seq.*, the face of the Contract (which is

[1] For ease of reference, Anderson Bros. Ford and Ford Motor Credit Company hereinafter will be referred to jointly as "Ford Credit".

the "disclosure statement" under the Act) contained certain disclosures. In paragraph 12, the Contract disclosed the security interest acquired by Ford Credit as follows:

> Security Interest: Seller shall have a security interest under the Uniform Commercial Code in the Property (described above) and in the proceeds thereof to secure the payment in cash of the Total of Payments and all other amounts due or to become due hereunder.

In paragraph 17 on the reverse side of the Contract,[2] captioned "RISK OF LOSS—INSURANCE," the Contract required the buyer to purchase and maintain in force physical damage insurance on the vehicle. Paragraph 17 also provided:

> *Buyer hereby assigns to Seller any monies payable under such [physical damage] insurance, by whomever obtained, including returned or unearned premiums,* and Seller hereby is authorized on behalf of both Buyer and Seller to receive or collect same, to endorse checks or drafts in payment thereof, to cancel such insurance or to release or settle any claim with respect thereto. The proceeds from such insurance, by whomever obtained, shall be applied toward replacement of the Property or payment of the indebtedness hereunder in the sole discretion of Seller. [Emphasis added.]

Under the assignment provision in the Contract italicized above, if the physical damage insurance policy on the vehicle is cancelled, any unearned premiums will be used to provide replacement insurance coverage or applied to the debt. The purpose of an assignment of unearned premiums in physical damage insurance is to assure the continued existence of the insurance on the vehicle during the life of the loan. Without the protection of such an assignment, debtors could cancel such insurance on financed

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[2] Although this paragraph is not numbered, it is referred to herein as "paragraph 17" since it comes between paragraph 16 and paragraph 18.

vehicles, thereby exposing lenders to the risk of uninsured collateral.

On May 3, 1978, the Buyers filed a two-count Complaint (J.A. 2-6) which alleged that Ford Credit violated the Truth in Lending Act and a similar Illinois statute because the Contract allegedly failed, *inter alia,* to disclose a security interest in returned or unearned physical damage insurance premiums (hereafter "unearned insurance premiums").

By an opinion issued on October 31, 1978, the District Court dismissed the Complaint in this action in its entirety for failing to state any claim for which relief could be granted. (J.A. 9-18). With respect to the assignment of unearned insurance premiums, the District Court reasoned:

> The assignment of unearned insurance premiums is not a security interest in the normal meaning of that term. Although provisions of the contract cannot control the meaning of statutory language or regulations, defendant is entitled to a usual and customary application of the words used in the contract between the parties as well as those in the official documents. (J.A. 11).

On November 17, 1978, the District Court issued a Supplemental Decision (J.A. 19-21) reinstating that portion of the Complaint which alleged that the assignment of unearned insurance premiums is a "security interest." The District Court based this reversal of its initial ruling on the decision in *Edmondson* v. *Allen-Russell Ford, Inc.,* 577 F.2d 291 (5th Cir. 1978), *cert. denied,* 441 U.S. 951 (1979). Thereafter, in a June 5, 1979 decision (J.A. 33-35) and an order entered on June 15, 1979 (J.A. 36-37), the District Court awarded summary judgment for Buyers holding that the assignment of unearned insurance premiums is a "security interest" that must be disclosed under the Act and Regulation Z.

On March 20, 1980, the United States Court of Appeals for the Seventh Circuit rendered the opinion (J.A. 38-64) as to which the writ of certiorari herein was granted, affirming the District Court's judgment of June 15, 1979. Judge Sprecher's opinion was accompanied by two expressly "reluctant" concurring opinions by Judges Cudahy and Swygert (J.A. 63-64) which noted in pertinent part that:

—the assignment provision at issue was "entirely incidental to the principal consumer credit transaction";

—requiring such a provision to be disclosed as a "security interest" on the face of the contract could not be taken as seriously suggesting a furtherance of the underlying purposes of the Truth in Lending Act;

—the opinion requires "the prominent disclosure of a rather esoteric right" which if disclosed as a "security interest" merely "add[s] virtually inconsequential information—lengthening, complicating and trivializing the disclosure for no apparent benefit"; and

—"the important ends of credit disclosure . . . [might] be obscured in a whirl of litigious gamesmanship" following the opinion.

SUMMARY OF ARGUMENT

The Act and Regulation Z require that "security interests" be disclosed on the front of retail installment contracts. The Regulation defines "security interest" but does not expressly provide whether the assignment provision at issue here constitutes such an interest. Therefore, it becomes necessary to turn to other sources in order to ascertain whether Congress intended to require disclosure of such provision.

The legislative history demonstrates that Congress did not intend to require disclosure of the assignment provision.

The purpose of the Act is to facilitate comparison shopping for credit by requiring uniform disclosure of credit terms, primarily those pertaining to the cost of credit. The security interest disclosure requirement was added to the Act so that a borrower would be informed of an essential term of the credit transaction—that his home was subject to a second mortgage. The rationale of that requirement does not extend to disclosure of the assignment provision which involves an incidental and ephemeral interest and does not affect the borrower's decision-making process in shopping for credit. Indeed, to require prominent disclosure of the assignment provision would tend to defeat the purpose of the Act by detracting from the credit cost disclosures which are of much greater importance to the borrower.

Enactment of the Truth in Lending Simplification and Reform Act (the "Simplification Act") on March 31, 1980 provides additional support for this conclusion. The legislative history of the Simplification Act expressly states that the disclosure of "incidental interests" such as an assignment of unearned insurance premiums is not required. With respect to this issue, the Simplification Act clarified existing law in order to correct overly technical judicial decisions that Congress believed had misinterpreted the original Act.

In *Ford Motor Credit Co.* v. *Milhollin*, 444 U.S. 555 (1980), this Court last term emphasized that great deference must be given to the interpretation of the Act and Regulation by the Federal Reserve Board (the "Board") and its staff. The Federal Reserve staff has recently issued a proposed Official Staff Interpretation under the present Act which holds that the assignment of unearned insurance premiums is not a security interest requiring disclosure.

If this Court were to rule that the assignment provision must be disclosed as a security interest, such ruling would establish a new principle of law and should be given pro-

spective application only (except as to the Buyers). There are millions of automobile credit contracts outstanding in the United States today, most of which contain an assignment of unearned insurance premiums on the reverse side. Retroactive application of an adverse ruling by this Court would thus lead to the imposition of staggering liability on consumer credit companies and banks without in any way furthering the purpose of the Act.

ARGUMENT

I. CONGRESS NEVER INTENDED TO REQUIRE DISCLOSURE OF AN ASSIGNMENT OF UNEARNED INSURANCE PREMIUMS.

A. The Act And Regulaton Z Do Not Expressly State Whether The Assignment Provision Is Required To Be Disclosed As A "Security Interest."

The Act requires "[a] description of any security interest held or to be retained or acquired by the creditor in connection with the extension of credit and a clear identification of the property to which the security interest relates." 15 U.S.C. § 1638(a)(10). The Act does not define the term "security interest." Regulation Z, 12 C.F.R. § 226.2(gg) (1980), provides that "security interest" means "any interest in property which secures payment or performance of an obligation." The Regulation also lists some examples of security interests required to be disclosed:

> security interests under the Uniform Commercial Code, real property mortgages, deeds of trust, and other consensual or confessed liens whether or not recorded, mechanic's, materialmen's, artisan's, and other similar liens, vendor's liens in both real and personal property, the interest of a seller in a contract for the sale of real property, any lien on property arising by operation of law, and any interest in a lease when used to secure payment or performance of an obligation.

The Regulation thus does not expressly cover the assignment provision at issue here.[3] The language of the Regulation, however, does make it clear that the Regulation focuses on security interests the function of which is to secure the debt—and not on interests in property which are incidental to the consumer transaction. Read with deference to the principle of *ejusdem generis*, Regulation Z would appear to halt the Act's disclosure requirement well short of the sort of incidental interest in property at issue here.

This case thus presents a situation similar to that recently considered by this Court in *Ford Motor Credit Co.* v. *Milhollin*, 444 U.S. 555 (1980). In *Milhollin*, the issue for decision was whether the Act required that the existence of an acceleration clause be disclosed on the face of a credit agreement. The Court first examined the express language of the Act and Regulation Z and concluded that the acceleration issue was "not governed by clear expression in the statute or regulation." *Id.* at 560.

As the Court noted,

> legislative silence is not always the result of a lack of prescience; it may instead betoken permission or, perhaps, considered abstention from regulation. In that event, judges are not accredited to supersede Congress or the appropriate agency by embellishing upon the regulatory scheme. Accordingly, caution must temper judicial creativity in the face of legislative or regulatory silence.

Id. at 565.

The express language of the Act and Regulation does not resolve the question of whether an assignment of unearned

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[3] As discussed below in Part II, the staff of the Board has taken the position that a creditor's right to unearned insurance premiums need *not* be disclosed as a security interest under the Act and Regulation.

insurance premiums must be disclosed as a security interest on the face of an installment credit contract. Therefore, as in *Milhollin,* "it becomes necessary to consider the implicit character of the statutory scheme." *Id.* at 560.

B. The Legislative History Of The Act Demonstrates That Congress Did Not Intend To Require Disclosure Of The Assignment Provision.

1. The Purpose of the Act is to Facilitate Comparison Shopping for Credit by Requiring Uniform Disclosure of Credit Terms.

The purpose of the Act is to "assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit. . . ." 15 U.S.C. § 1601(a). As was made clear in the legislative history of the Act, the primary emphasis was on assuring the disclosure of the *cost of credit* in uniform terms:

> The basic purpose of the truth in lending bill is to provide a full disclosure of *credit charges* to the American consumer . . . .
>
> By providing full and comparable disclosure information, the bill will permit consumers to compare the *cost of credit* among different creditors and to shop effectively for the best credit buy. The committee also believes that the bill will promote the wiser use of consumer credit by consumers when they know the full *cost of credit.* [Emphasis added.]

Report of the Senate Committee on Banking and Currency to accompany S. 5, S.Rep. No. 392, 90th Cong., 1st Sess. 1 (1967). *Accord,* Report of the House Committee on Banking and Currency to accompany H.R. 11601, H.R. Rep. No. 1040, 90th Cong., 1st Sess. 6-7 (1967), *reprinted in* [1968] U.S. Code Cong. & Ad. News 1962, 1962-63.

2. The Security Interest Disclosure Requirement was Added to the Act in Order to Curb Abuses Relating to Second Mortgages on Borrowers' Homes.

Neither the 1967 Senate bill nor the 1967 House bill made any reference to the disclosure of security interests taken in connection with consumer credit transactions. The provision of the Act relating to security interest disclosure was proposed as an amendment from the floor of the House of Representatives by Congressman Cahill of New Jersey. 114 Cong. Rec. 1610 (1968). That amendment was one of four amendments offered by Mr. Cahill for the purpose of curbing perceived abuses and deceptive practices in connection with consumer loans secured by second mortgages.[4]

Mr. Cahill stated that his amendments were designed to strengthen the bill then before the House with respect to mortgage lending abuses:

> [D]espite the general comprehensiveness of this legislation, in my judgment there are serious and important omissions which should be corrected. These omissions relate primarily to consumer credit extended on the security of mortgages and liens on homes and residences. I am sure that most of the Members are aware of the extent to which vicious secondary mortgage schemes have victimized homeowners. . . .
>
> • • • •
>
> I have, therefore, offered these four amendments designed to improve the truth-in-lending provisions with respect to mortgage transactions.

[4] The other amendments offered by Congressman Cahill were intended to extend the disclosure requirements of the Act to mortgage brokers and others who arrange credit transactions; to permit actions to be brought against assignees of mortgages in certain circumstances; and to provide that a borrower whose residence is put up as security shall receive the required disclosures at least three days before the transaction is consummated. 114 Cong. Rec. 1610-11 (1968).

114 Cong. Rec. 1611 (1968). With respect to security interest disclosure, Mr. Cahill explained that there was a need to require creditors to disclose security interests acquired in connection with a consumer credit transaction in order to avoid situations in which the homeowner "is never informed nor aware that his *home* is being made *subject to a mortgage.*" *Id.* (Emphasis added.) Mr. Cahill summarized the intended effect of his amendment by stating that it "would require that there be disclosure that a *mortgage* is being placed *on the borrower's home* and that the consequences of such a mortgage can be explained." *Id.* (Emphasis added.)

Mr. Cahill's amendments were adopted without objection by the House. 114 Cong. Rec. 1610-11 (1968). Senator Proxmire, in bringing the amendments to the attention of the Senate, described the security interest disclosure requirement as follows:

> Congressman Cahill, of New Jersey, has offered an important amendment to the truth-in-lending bill which tightens up on the *second mortgage racket*. . . . Second, it would require a disclosure of the fact that credit is being secured by a *mortgage* on the homeowner's property. . . . [Emphasis added.]

114 Cong. Rec. 5024 (1968). With no further discussion of the security interest disclosure requirement, the provision was incorporated into the final version of the Act and adopted into law as 15 U.S.C. § 1638(a)(10).

The security interest disclosure requirement thus was designed to prevent certain deceptive practices in credit transactions in which a borrower takes out a second mortgage on his home to secure the loan. The purpose of the disclosure is to inform a borrower that his property is serving as security for the loan and thus is at risk should he fail to repay the loan. Federal Reserve Board Staff Opinion No. 1066, [1974-77 Special Releases Transfer Binder]

CONS. CRED. GUIDE (CCH) ¶ 31,406 (June 4, 1976). Congress determined that a consumer, in order to comparison shop for the best credit terms, should be told whether or not a lender would require him to put his home at risk. It therefore required that lenders disclose, on the face of the contract, this essential term.

In the transaction in the instant case, the automobile purchased by the Buyers is analogous to a home subject to a second mortgage; it served to secure the extension of credit and was at risk if the Buyers failed to make the required monthly payments. Therefore, the fact that Ford Credit retained a security interest in the automobile had to be (and was) disclosed to the Buyers pursuant to 15 U.S.C. § 1638(a)(10). But it would stretch the rationale of that section beyond the breaking point to hold that an assignment of unearned insurance premiums is analogous to a home mortgage. The right to receive unearned insurance premiums is hardly an essential term, and it is wholly unrelated to the borrower's ability to repay the underlying debt. The very existence of the unearned premiums depends upon the cancellation of the insurance coverage, a decision unrelated to, and not necessarily triggered by, a default in payment of the debt.

Moreover, from the moment of issuance of physical damage insurance which names the lender as a loss payee, the property interests in the policy are at least joint, and in fact belong more to the lender than the debtor as long as the debt remains unpaid. In *Rounds* v. *Community National Bank,* 454 F. Supp. 883, 888 (S.D. Ill. 1978), the court observed:

> Both the assignment of unearned premiums and the assignment of insurance proceeds do provide some benefit and protection to the lender. But neither of

> those provisions subject the debtor's property to any lien or any risk. Rather, the insurance provisions of the agreement are properly construed as being mutually protective of the interests of both the debtor and the creditor.

Disclosure of the assignment of unearned insurance premiums as a security interest simply would not serve the purpose for which such disclosures are required by the Act—to let the borrower know what property belonging to him will be reachable on default.

3. The Act and Regulation Require Certain Insurance Information—But Not Information Relating to Unearned Insurance Premiums—to be Included in the Disclosure Statement.

Before adopting the Act, Congress carefully considered what information regarding insurance aspects of credit transactions ought to be included in Truth in Lending disclosure statements. The primary issue facing Congress in this area was whether premiums paid by consumers for various types of insurance should be included in the "finance charge" stated in the disclosure statement. With respect to property damage insurance on property securing the debt, Congress determined to permit creditors to exclude the premiums from the finance charge, but only if the debtor was clearly informed of his right to choose where to buy the insurance:

> Charges or premiums for insurance, written in connection with any consumer credit transaction, against loss of or damage to property or against liability arising out of the ownership or use of property, shall be included in the finance charge unless a clear and specific statement in writing is furnished by the creditor to the person to whom the credit is extended, setting forth the cost of the insurance if obtained from or through the creditor, and stating that the person to whom the

> credit is extended may choose the person through which the insurance is to be obtained.[5]

15 U.S.C. § 1605(c). *See also* 12 C.F.R. § 226.403.

The statutory scheme with respect to property damage insurance disclosures is clearly relevant in ascertaining Congressional intent with respect to disclosure of unearned premiums on such insurance. In *Shanks* v. *Greenbriar Dodge, Inc.*, No. (75-1154A) (N.D. Ga. 1976),[6] *rev'd* 577 F.2d 296 (5th Cir. 1978), the district court found that Congress did not require even the total cost of property damage insurance premiums to be itemized, disclosed or included in the finance charge. Therefore, the court reasoned, it makes little sense to interpret the Act as requiring that the assignment of unearned insurance premiums be disclosed:

> Congress and the Board have given considerable study to the cost of insurance incident to the obtaining of credit and have specifically set out those disclosures which it was felt effectuated the policy of the Act. As both bodies have thoroughly considered the insurance premium issue and have not required the disclosure sought here, then this Court should not.

Moreover, even the fact that the borrower is required to maintain property damage insurance need not be included in the disclosure statement. *Mullen* v. *North Pacific Bank*, 610 P.2d 949, 954 (Wash. App. 1980).

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[5] For example, Ford Credit's form of contract contains the following statement on the front side, about half-way down the left column:

> NOTICE TO BUYER: . . . (2) You have the right to choose the person through whom the Physical Damage Insurance required under this contract is to be obtained.

[6] The district court's unreported opinion in *Shanks* is reproduced in the Addendum of Legal Authorities ("Add.") attached to this brief, at Add. 40-52.

Thus, in deciding to focus the Act's disclosure requirements on the cost and essential terms of credit, Congress concluded that the cost of property damage insurance premiums need not always be included in the disclosure statement. Indeed, even the fact that the borrower is required to maintain such insurance need not be so disclosed. Yet, an assignment of the unearned portion of property damage insurance premiums is clearly of less importance to a borrower than the total cost of such insurance premiums or the fact that such insurance is required as part of the transaction. In most circumstances, the unearned portion of the insurance premiums will be substantially smaller than the total cost since the premiums will be earned during the time that the insurance coverage remains in force. Further, unearned insurance premiums will be rebated only in the distinct minority of cases in which the insurance coverage is cancelled before the end of the period for which the premiums were paid. Therefore, since Congress determined that it was not necessary to include in the disclosure statement the fact that the borrower is required to maintain property damage insurance or always to include the total cost of such insurance premiums, it is most unlikely that Congress intended to require that the less important assignment of unearned insurance premiums be so disclosed.

4. Disclosure of the Assignment Provision as a Security Interest Would Frustrate the Purpose of the Act.

The contracts used in these transactions already contain so much information that Judge Moore, dissenting in *Mirabal* v. *General Motors Acceptance Corp.*, 537 F.2d 871, 888 (7th Cir. 1976), noted that if the entire contract were printed on only one side, it would be "an unwieldy document of some 30 inches in length—not unlike an ancient Egyptian papyrus scroll." Requiring too much detail to be

included in disclosure statements can thus defeat the purpose of the Act because the disclosure statements become unreadable. As this Court recognized in *Milhollin*:

> The concept of "meaningful disclosure" that animates TILA [citation omitted] cannot be applied in the abstract. *Meaningful* disclosure does not mean *more* disclosure. Rather, it describes a balance between "competing considerations of complete disclosure . . . and the need to avoid . . . [information overload]." [Citations omitted.]

444 U.S. at 568. The Board, in explaining its recently proposed revision of Regulation Z, similarly observed that the "impact and utility" of disclosure statements are "diluted" to the extent that essential information is accompanied by "complex disclosure of less significant terms." 45 Fed. Reg. 80647, 80648 (Dec. 5, 1980).

Application of these principles to the issue in this case demonstrates that the decision below is likely to frustrate the purpose of the Act. Requiring disclosure of the assignment provision (as well as a listing of all other incidental interests in property which a lender may acquire in a credit transaction) to be added to the straightforward language in paragraph 12 on the front of the Contract would only distract the debtor from the important fact that the financed automobile (the *real* "security") and the proceeds therefrom were at risk if he failed to make the periodic payments due under the Contract. The fact that the debtor assigned unearned insurance premiums, if any,[7] to the lender, to be

[7] In the vast preponderance of cases, unearned premiums are never collected by the creditor because they are earned during the life of the installment contract and the coterminous physical damage insurance policy. In the case at bar, there were no unearned insurance premiums since the Buyers never paid any premiums. (Rec. Doc. No. 33 at 46).

applied by the lender either to replace the insurance or to pay down the debtor's loan obligation is of virtually no consequence to the debtor. It does not place his property at risk, and giving it the same dignity of disclosure as a security interest can only result in confusion.

Moreover, inclusion of the assignment provision on the front side of credit contracts would not aid consumers in shopping for credit. With respect to the precise question at issue here, the Federal Reserve staff recently published a proposed interpretation which stated (Add. 56):

> Truth in Lending disclosures are meant to provide useful information to consumers to enhance credit shopping. . . . We believe that information regarding the creditor's interest in insurance proceeds and unearned premiums would not be used in comparison shopping.

Proposed Official Staff Interpretation FC-0173 (Add. 54-57), 45 Fed. Reg. 63295 (Sept. 24, 1980).

Professor Jonathan Landers explained why such technical contract terms are not considered by consumers in their decision-making process:

> [T]he technical terms of the contract tend to be relatively standardized and do not lend themselves to either comparison shopping or effective bargaining. This is because the economic effect of the technical terms is small and consumers who do compare may be expected to shop or bargain on the key cost items—the finance charge and the APR [annual percentage rate]—and not on a variety of subsidiary terms.

J. Landers, *Some Reflections on Truth in Lending*, 1977 U. Ill. L.F. 669, 685. Therefore, to require prominent disclosure of the insignificant assignment provision at issue here would not further the purpose of the Act by facilitating comparison shopping for credit. Rather, such requirement would tend to defeat the purpose of the Act by detracting

from the credit cost disclosures which are of much greater importance to the consumer.

C. The Legislative History Of The Simplification Act Confirms That Congress Intended Not To Require Disclosure Of The Assignment Provision.

1. Such Disclosure is Not Required under the Simplification Act.

As noted above, Congress intended the Act to promote "meaningful disclosure of credit terms." However, in recent years Congress became concerned that overly technical judicial decisions were defeating that purpose by requiring too much complexity in disclosure statements. This concern was expressed in the Report of the Senate Committee on Banking, Housing and Urban Affairs, S. Rep. No. 96-73, 96th Cong., 1st Sess. 2 (1979), *reprinted in* [1980] U.S. Code Cong. & Ad. News 878, 879 (May 1980 Supp.):

> There is considerable evidence, for example, that disclosure forms given consumers are too lengthy and difficult to understand. Creditors, on the other hand, have encountered increasing difficulty in keeping current with a steady stream of administrative interpretations and amendments, as well as *highly technical judicial decisions.* [Emphasis added.]

Because of such decisions, creditors had felt compelled to issue lengthy disclosure statements "written in legalistic fine print . . . instead of the simple, concise disclosure form Congress intended." *Id.* at 3, [1980] U.S. Code Cong. & Ad. News at 879-80.

In response to these concerns, the Simplification Act was adopted and signed into law on March 31, 1980 as Title VI of P.L. 96-221, 94 Stat. 132, 168. Under Section 614(a)(9) of the Simplification Act, 94 Stat. 179, where the credit is secured, the creditor shall disclose "a statement that a secu-

rity interest has been taken in (A) the property which is purchased as part of the credit transaction, or (B) property not purchased as part of the credit transaction identified by item or type."

The legislative history makes it clear that the disclosure of "incidental interests," such as an assignment of unearned insurance premiums, is *not* required:

> When a security interest is being taken in property not purchased as part of the credit transaction, the Committee intends this provision to require a listing by item or type of the property securing the transaction, *but not a listing of related or incidental interests in the property.* For example, a loan secured by an automobile (not being purchased with the proceeds of the loan) would require a statement indicating that the loan is secured by an automobile *but would not require a listing of incidental or related rights which the creditor may have such as insurance proceeds or unearned insurance premiums,* rights arising under, or waived in accord with state law, accessions, accessories, or proceeds. [Emphasis added.]

S. Rep. No. 96-368, 96th Cong., 1st Sess. 30 (1979), *reprinted in* [1980] U.S. Code Cong. & Ad. News 834, 864 (May 1980 Supp.).

The Simplification Act, which becomes effective on April 1, 1982, requires the Board to have implementing regulations in place by April 1, 1981. 94 Stat. 185. The Board recently issued a proposed revision of Regulation Z in response to that mandate. 45 Fed. Reg. 80647 (Dec. 5, 1980). The term "security interest" is defined in the proposed revision to mean

> an interest in property that secures performance of a consumer credit or lease obligation and that is recognized by or enforceable under state or federal law. *It does not include incidental interests such as* an interest

> in proceeds, assessions, additions, fixtures, *insurance proceeds or premium rebates* . . . . [Emphasis added.]

Id. at 80696. The Board noted that this definition is intended to implement the Congressional intent, evidenced by the language quoted above from the Senate Report, to restrict security interest disclosure to a simple but meaningful concept. *Id.* at 80655. The Board also observed that this definition "explicitly excludes from coverage many incidental interests in property that have been found to be security interests by various courts in the past." *Id.*

2. With Respect to this Issue, the Simplification Act Clarifies Existing Law.

Although the Simplification Act had many purposes, this amendment was designed to clarify Congress' original intent in adopting the Act. Senator Garn, one of the principal authors of the Simplification Act, specifically indicated that the amendment simply clarified existing law:

> Many cases have resulted from the complex security interest disclosure requirements under the law. An illustrative case is *Gennuso* v. *Commercial Bank and Trust Company,* 455 F. Supp. 461 (W.D. Pa 1976); 566 F.2d 437, (3rd Cir. 1977), which required the creditor's right in property insurance proceeds and unearned property insurance premiums to be disclosed as a "security interest". *Although as presently written the law does not require that result, S. 108 should prevent such ludicrous interpretations* by requiring merely a positive indication if a security interest is being taken in the property purchased and if it is in property not being purchased in the transaction, simply a general listing of the type of property without a listing of incidental related interests. [Emphasis added.]

125 Cong. Rec. S4990 (daily ed. May 1, 1979).

The Board also regards the provisions of the Simplification Act concerning security interest disclosure as clarify-

ing the intent of the original Act. According to the Board's analysis, the effects of the Simplification Act can be put into five categories, one of which is the clarification of "certain complex legal questions that have produced conflicting court decisions in the past." 45 Fed. Reg. at 80731 (Dec. 5, 1980). The Board specifically noted that one of the legal issues which was clarified by the Simplification Act is "adequate disclosure of security interests." *Id.* at 80733.

This Court has repeatedly recognized that "subsequent legislation reflecting an interpretation of an earlier act is entitled to great weight in determining the meaning of the earlier statute." *Regents of University of California* v. *Bakke,* 438 U.S. 265, 349 (1978) (opinion of Justices Brennan, White, Marshall and Blackmun). *Accord, NLRB* v. *Bell Aerospace Co.,* 416 U.S. 267, 275 (1974); *Red Lion Broadcasting Co.* v. *FCC,* 395 U.S. 367, 380-81 (1969).

The Court recently applied this principle in *Seatrain Shipbuilding Corp.* v. *Shell Oil Co.,* 444 U.S. 572 (1980), which involved the construction of a section of the Merchant Marine Act. The Court examined first the language of the statute and the original legislative history, but found no evidence that Congress had addressed the precise question before the Court. The Court then examined the legislative history of subsequent amendments to the statute and found that a later Congress had expressed a clear understanding of how the question was to be treated under the original statute. The Court adopted the interpretation of the later Congress, noting that

> while the views of subsequent Congresses cannot override the unmistakable intent of the enacting one, . . . such views are entitled to significant weight, . . . and particularly so when the precise intent of the enacting Congress is obscure. [Citations omitted.]

444 U.S. at 596. In the instant case, the Simplification Act, reflecting Congress' interpretation of the original Act, is

thus entitled to great weight in establishing that Congress did not require disclosure of the assignment provision as a security interest under the original Act.

D. Although The Judicial Decisions On This Issue Are Sharply Divided, The Courts Which Have Looked To The Purpose Of The Act Have Held That The Assignment Provision Need Not Be Disclosed As A Security Interest.

Since prior to the adoption of the original Act in 1968, virtually the entire consumer credit industry has disclosed the retention of incidental interests in insurance on financed collateral on the back of installment contracts. *See* the brief filed herein by *amici curiae* Consumer Bankers Association, General Motors Acceptance Corporation and National Consumer Finance Association. Because incidental interests in insurance were not regarded as being within the ambit of "security interests" required to be disclosed under the Act, this form of disclosure has continued to be used in millions of credit transactions involving billions of dollars. Yet, it was not until 1976 that the first case alleging that such form of disclosure violated the Act was decided. Once invented, however, theories of technical violations of the Act tend to wash across the country in waves as plaintiffs (and their counsel) seek to recover the penalties provided by the Act. As a new claim—no matter how novel—begins to appear in reported cases, the wave begins to expand and pick up force and intensity.[8]

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[8] More than 13,000 lawsuits under the Act had been filed in the federal courts as of June 30, 1979. The Board recently stated that much of this litigation "concerned aspects of disclosures apart from credit cost disclosures, the critical elements of Truth in Lending according to Congress. Notable among disputed areas in the late 1970's were identity of the creditor, security interest issues, disclosure of loan proceeds, acceleration clause issues, and issues of rescission." 45 Fed. Reg. 80732 (Dec. 5, 1980).

The question of whether an assignment of unearned insurance premiums and insurance proceeds must be disclosed as a security interest under the Act is such a wave, which first formed in the Northern District of Georgia in 1976. Since then, the question has been much litigated, and the cases are sharply divided.[9] These conflicting decisions have created strong cross-currents on this issue which present the danger of white water rapids for creditors who must conform their contract forms to the law or face stiff penalties. Ford Credit submits that the reason for the conflicting decisions is that a number of courts have failed to look to the Congressional purpose underlying the Act.

The first district court decisions within the Northern District of Georgia reached opposite results. In *Edmondson* v. *Allen-Russell Ford, Inc.*, No. C75-940A (N.D. Ga. 1976) (Add. 18-26), the district court held that an assignment of unearned insurance premiums was a security interest which must be disclosed. However, that decision was soon fol-

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[9] Cases holding that such assignment must be disclosed as a security interest include: *Souife* v. *First National Bank of Commerce*, 628 F.2d 480 (5th Cir. 1980), *pet. for reh. en banc pend.* (Add. 53); *Murphy* v. *Ford Motor Credit Co.*, 629 F.2d 556 (8th Cir. 1980); the Seventh Circuit's decision below; *Edmondson* v. *Allen-Russell Ford, Inc.*, 577 F.2d 291 (5th Cir. 1978), *cert. denied*, 441 U.S. 951 (1979); *Gennuso* v. *Commercial Bank & Trust Co.*, 566 F.2d 437 (3d Cir. 1977); *Hagler* v. *Ford Motor Credit Co.*, 381 So.2d 80 (Ala. App. 1980); and *Luczak* v. *General Motors Acceptance Corp.*, 494 F.Supp. 210 (W.D.N.Y. 1980).

Cases holding that such assignment need not be disclosed as a security interest include: *James* v. *Ford Motor Credit Co.*, ____ F.2d ____ (10th Cir. 1980) (Add. 27-39); *Mullen* v. *North Pacific Bank*, 610 P.2d 949 (Wash. App. 1980); *Ancrum* v. *Charleston Lincoln Mercury, Inc.*, No. 78-804 (D.S.C. 1980) (Add. 1-10); *Ector* v. *Southern Discount Co.*, No. C78-899A (N.D. Ga. 1980) (Add. 11-17); and *Rounds* v. *Community National Bank*, 454 F.Supp. 883 (S.D. Ill. 1978).

lowed by a contrary holding from the same district in *Shanks* v. *Greenbriar Dodge, Inc.*, No. C75-1154A (N.D. Ga. 1976) (Add. 40-52). The Fifth Circuit affirmed *Edmondson*, 577 F.2d 291 (5th Cir. 1978), and reversed *Shanks*, 577 F.2d 296 (5th Cir. 1978), without discussing whether the result it reached was consistent with Congressional intent or would further the purpose of the Act.

This pattern of conflicting holdings is also illustrated by the decisions of the lower courts in the Seventh Circuit. In *Rounds* v. *Community National Bank*, 454 F. Supp. 883, 888 (S.D. Ill. 1978), the court held that the assignment provision was not a Truth in Lending security interest:

> The provisions impose no claim against, nor risk to, the plaintiff's assets. If such ephemeral interests are to be deemed to be security interests within the disclosure requirements of the Act, that determination should emanate from Congressional enactment or from a determination of the Board, not from a judicial decree.

As discussed above in the Statement of the Case, the first opinion of the district court in this case likewise held that the assignment provision is not a security interest. (J.A. 10-12). However, the district court vacated its first opinion and reversed its position based upon the Fifth Circuit's decision in *Edmondson*. (J.A. 19-21).

The Seventh Circuit, in the decision below, held that the Act was violated by a failure to disclose an assignment of unearned insurance premiums as a security interest, but conceded that such violation was, at worst, "purely technical." (J.A. 50). The Seventh Circuit apparently felt compelled to apply a highly technical reading of the definition of "security interest" in Regulation Z, without regard to whether or not the result it reached would further the purposes of the Act. This point was candidly expressed in the concurring opinion of Judge Cudahy:

> I do not read it [the panel opinion] as seriously suggesting that the result we reach furthers the underlying purposes of the Truth in Lending Act. . . .
>
> Here we require the prominent disclosure of a rather esoteric right to unearned premiums for physical damage insurance (protecting both the seller's and the buyer's interest in the property), which may be used to provide replacement insurance coverage or applied against the buyer's debt in the event of cancellation of the insurance. This "security interest" is normal in the circumstances, but is entirely incidental to the principal consumer credit transaction. Primarily, it assures maintenance of the insurance and is not necessarily even related to default on the principal debt.
>
> To disclose this "security interest" on the *face* of the contract (which is the point here) is merely to add virtually inconsequential information—lengthening, complicating and trivializing the disclosure for no apparent benefit. (J.A. 63).

Enactment of the Simplification Act on March 31, 1980 should have put an end to this controversy, since, as discussed above, the legislative history of the Simplification Act made clear that Congress had never intended to require disclosure of the assignment provision. Relying upon those expressions of legislative intent, certain courts have held that the assignment provision need not be disclosed as a security interest. Other courts, however, have refused to defer to these explicit statements of Congressional intent and have persisted in enforcing a requirement which Congress never intended to impose.

The first decision to consider the Congressional intent expressed in the legislative history of the Simplification Act was *James* v. *Ford Motor Credit Co.*, __ F.2d __ (10th Cir. 1980) (Add. 27-39). Relying upon the legislative history and this Court's recent *Milhollin* decision, the Tenth Circuit held that "the Act does not require, and Congress did not

intend it to require, an exemplification of that interest [in unearned insurance premiums] on the face of the installment contract." (Add. 33). In its order denying the petition for rehearing, the court in *James* explained that, in accordance with this Court's precedents dealing with statutory construction, it had used the Simplification Act as an aid in determining the meaning of the present Act. (Add. 38-39).

In *Ancrum* v. *Charleston Lincoln Mercury, Inc.*, No. 78-804 (D.S.C. Aug. 19, 1980) (Add. 1-10), the court endorsed the approach taken by the Tenth Circuit in *James*:

> The inclusion of the assignment of unearned or returned insurance premiums and insurance proceeds would provide the consumer with "information overload". . . . The decision [in *James*] recognizes and enhances the intent of Congress to provide the consumer with a meaningful, non-technical, simple and concise disclosure. I therefore conclude that the assignment of insurance proceeds and unearned or returned insurance premiums do [sic] not constitute a security interest which is required to be disclosed on the face of the contract. (Add. 7).

The court in *Ancrum* distinguished the contrary holdings of *Gennuso, Edmondson* and *Valencia* on the ground that those decisions were rendered prior to enactment of the Simplification Act. (Add. 4).

The Eighth Circuit reached the opposite result in *Murphy* v. *Ford Motor Credit Co.*, 629 F.2d 556 (8th Cir. 1980), holding that the assignment provision had to be disclosed as a security interest on the face of the installment contract. The court refused to be guided by the intent of Congress expressed in the Simplification Act on the ground that the Simplification Act would not take effect for two years. *Id.* at 560. The court's analysis thus completely missed the

point that the Simplification Act was intended in pertinent part to clarify Congress' intent in the original Act and to correct the "highly technical judicial decisions" that Congress believed had misinterpreted the original Act.

The most recent appellate decision on this issue was *Souife* v. *First National Bank of Commerce,* 628 F.2d 480 (5th Cir. 1980), in which a Fifth Circuit panel declined to overrule *Edmondson* even in light of the expressions of Congressional intent found in the legislative history of the Simplification Act.[10] The panel's analysis of the legislative history of the Simplification Act is fundamentally wrong. For example, the court quoted the remarks of Senator Garn, which included the following statement pertaining to *Gennuso* v. *Commercial Bank & Trust Co.,* 566 F.2d 437 (3d Cir. 1977) (requiring disclosure of the assignment provision as a security interest):

> "Although as presently written the law does not require that result, S.108 should prevent such ludicrous interpretations. . . ."

628 F.2d at 484, *quoting* 125 Cong. Rec. S4990 (daily ed. May 1, 1979). The court then reached the astounding conclusion that those remarks did not indicate "that cases like *Edmondson* and *Gennuso* incorrectly interpreted the original Act." 628 F.2d at 484. The conclusion flies in the face of the language used by Senator Garn. Senator Garn characterized *Gennuso* as a "ludicrous interpretation" of the Act and clearly stated that the original Act did not require disclosure of the assignment provision. Thus, the Fifth Circuit panel failed to heed this Court's admonition in *Milhollin* that courts are not free to "embellish upon the reg-

[10] In an order entered December 5, 1980, however, the Fifth Circuit announced that it would defer consideration of the bank's petition for rehearing en banc pending this Court's decision in the instant case. (Add. 53).

ulatory scheme" by imposing penalties on creditors for non-disclosure of matters which are not required to be disclosed under the Act. 444 U.S. at 565.

In *Souife,* the Fifth Circuit panel also quoted the statement in the Senate Report that

> "a loan secured by an automobile (*not being purchased with the proceeds of the loan*) would require a statement indicating that the loan is secured by an automobile but would not require a listing of incidental or related rights which the creditor may have such as insurance proceeds or unearned insurance premiums. . . ." [Emphasis added.]

628 F.2d at 484, *quoting* S. Rep. No. 96-73, 96th Cong., 1st Sess. 16 (1979). The court attempted to distinguish this statement on the basis of the phrase italicized above since the automobile in the transaction before it had been purchased with the proceeds of the loan. 628 F.2d at 485. However, that distinction makes no difference. Under Section 614(a)(9) of the Simplification Act, 94 Stat. 179, the disclosure statement in a secured transaction must contain

> a statement that a security interest has been taken in (A) the property which has been purchased as part of the credit transaction, or (B) property not purchased as part of the credit transaction identified by item or type.

Thus, the statement quoted above from the Senate Report referred specifically to an automobile not purchased with the loan proceeds because it was describing the operation of Section 614(a)(9)(B). However, the same result would follow under Section 614(a)(9)(A), which requires only a statement that a security interest has been taken in the property purchased in the credit transaction. The Senate Report clearly states that the required disclosure of prop-

erty securing the loan need not include a listing of "incidental or related rights" such as an assignment of unearned insurance premiums. As discussed *supra* at pp. 20-21, the Board quoted this language from the Senate Report in support of its definition of "security interest" in the proposed revision of Regulation Z which excluded an assignment of unearned insurance premiums in *all* situations. There is no conceivable reason, and the Fifth Circuit panel in *Souife* suggests none, why such "incidental or related rights" must be disclosed with respect to property purchased with the loan proceeds, but not with respect to property purchased from other funds.

Thus, the pattern of conflicting judicial decisions is continuing, even in the face of the explicit statements of Congressional intent found in the legislative history of the Simplification Act. Only a decision from this Court can resolve the conflict and provide the credit industry with the guidance it needs on this issue.

E. Creditors Should Not Be Subject To The Penalties Imposed By The Act For Conduct Not Clearly Proscribed In The Act.

Under the Act a civil penalty is imposed upon a creditor for an amount equal to double the amount of the finance charge (up to a $1,000 maximum) for a violation of the Act. 15 U.S.C. § 1640(a). While the Act has been viewed as remedial in nature, the statute also imposes what are clearly penalties, as Congress has recognized in the body of the Act itself. Section 113 of the Act, 15 U.S.C. § 1612, expressly recognizes that the civil recovery provided for under Section 1640(a) is a "penalty". This Court noted in *Mourning* v. *Family Publications Service, Inc.*, 411 U.S. 356, 375 (1973), that the Act contained penal sanctions, but found that the risk of imposing a penalty without first

giving fair warning of what conduct was prohibited was not present in that case because the language of the challenged rule was explicit. However, in the case at bar, the language of the Regulation is not at all clear, as demonstrated by the sharply conflicting interpretations of the courts.

Fundamental fairness and equity dictate that lenders not be held liable under the penal sanctions of the Act for conduct not clearly proscribed in the Act. Such sanctions should not be imposed under the guise of liberally construing the legislation, especially where, as here, the intent of Congress is not furthered by imposing the penalty. As discussed above, the purpose of the Act—to permit borrowers to comparison shop for credit—would be retarded by requiring disclosure of an incidental and transitory interest in unearned insurance premiums as a security interest.

II. THE FEDERAL RESERVE BOARD DOES NOT REQUIRE DISCLOSURE OF AN ASSIGNMENT OF UNEARNED INSURANCE PREMIUMS.

A. Great Deference Must Be Given To The Interpretations Of The Act And Regulation By The Board And Its Staff.

This Court has frequently held that the interpretation of a statute by the agency responsible for its administration is entitled to great deference. *E.g., Zenith Radio Corp.* v. *United States,* 437 U.S. 443, 450 (1978); *Mourning* v. *Family Publications Service, Inc.,* 411 U.S. 356, 371-72 (1973). When, as here, the construction of an administrative regulation rather than a statute is in issue, deference to the agency's interpretation is even more clearly in order. Indeed, such interpretation is controlling unless plainly erroneous or inconsistent with the regulation. *United States* v. *Larionoff,* 431 U.S. 864, 872 (1977); *Udall* v. *Tallman,* 380 U.S. 1, 16-17 (1965).

In *Ford Motor Credit Company* v. *Milhollin*, 444 U.S. 555, 565-68, this Court recently emphasized the need to defer to the Federal Reserve Board's interpretation of the Act and Regulation Z:

> [D]eference [to the views of the administrative entity appointed to apply and enforce a statute] is especially appropriate in the process of interpreting the Truth in Lending Act and Regulation Z. . . .
>
> . . . The Act is best construed by those who give it substance in promulgating regulations thereunder.
>
> Furthermore, Congress has specifically designated the Federal Reserve Board and staff as the primary source for interpretation and application of truth in-lending-law. . . .
>
> • • • •
>
> Finally, wholly apart from jurisprudential considerations or congressional intent, deference to the Federal Reserve is compelled by necessity; a court that tries to chart a true course to the Act's purpose embarks upon a voyage without a compass when it disregards the agency's views.

The Court also held that the same degree of deference should be accorded to the views of the Federal Reserve staff: "Unless demonstrably irrational, Federal Reserve Board staff opinions construing the Act or Regulation should be dispositive. . . ." 444 U.S. at 565.

B. Proposed Official Staff Interpretation FC-0173 Expressly Holds That The Assignment Provision Need Not Be Disclosed As A Security Interest.

The Federal Reserve staff has recently issued a proposed Official Staff Interpretation which interprets 12 C.F.R. §§ 226.2(gg) and 226.8(b)(5) of the *present* Regulation and holds that the assignment of unearned insurance premiums

is *not* a security interest requiring disclosure under the Act. Proposed Official Staff Interpretation FC-0173 (Add. 54-57), 45 Fed. Reg. 63295 (Sept. 24, 1980). Recognizing that its interpretation is directly contrary to several circuit court decisions, the Federal Reserve staff stated that this interpretation better serves the purposes of the Act:

> The staff believes that *a creditor is not required* by this section [Regulation Z, 12 C.F.R. § 226.8(b)(5) (1980)] *to disclose its right to receive insurance proceeds or unearned insurance premiums* nor to disclose that it is named as loss payee or beneficiary on an insurance policy. Truth in Lending disclosures are meant to provide useful information to consumers to enhance credit shopping. Consumers do need to know that they risk the loss of certain property if they default. The disclosures under § 226.8(b)(5) inform consumers of which property is subject to that risk at the time the credit decision is being made. We believe that information regarding the creditor's interest in insurance proceeds and unearned premiums would not be used in comparison shopping. *Although a technical reading of the security interest definition might cover a creditor's interest in insurance proceeds and unearned premiums, it is our opinion that such incidental interests are not the type of interests meant to be covered by § 226.8(b)(5).*
>
> The staff recognizes that there are a number of circuit court decisions to the contrary. We believe, however, that our position better serves the purpose of the statute and the regulation to convey in a meaningful way information that can be used by consumers in shopping for credit. (Add. 56) [Emphasis added.]

This interpretation clearly is a rational response to those overly technical judicial decisions, discussed above, which imposed liability on creditors without furthering the purpose of the Act.

The fact that a staff interpretation such as this is issued after a credit transaction is consummated does not alter the deference to be given to such interpretation. In *Milhollin*, this Court considered whether certain credit contracts executed before 1976 violated the Act. Relying upon an Official Staff Interpretation issued in 1977, this Court upheld the form of disclosure used by Ford Credit with respect to contracts which predated the Official Staff Interpretation. 444 U.S. at 563-65 and 567, n.11.

The staff recently announced that it has determined to defer final action on the proposed interpretation pending this Court's decision in the instant case. 45 Fed. Reg. 84074 (Dec. 22, 1980) (Add. 58). That action in no way represents a change in the Board's or the staff's position on the merits of this issue. Rather, it reflects a long-standing reluctance on the part of the Board and its staff to get involved in pending private litigation. *See* Federal Reserve staff letters dated January 9, 1970 and October 22, 1970, [1969-74 Special Releases Transfer Binder] CONS. CRED. GUIDE (CCH) ¶¶ 30,261 and 30,596. In these circumstances, it is still appropriate to give great weight to the informed judgment of the Board and its staff—as expressed in the proposed revision of Regulation Z (*see* pp. 20-22, *supra*) as well as in proposed interpretation FC-0173—that the assignment provision at issue here need not be disclosed as a security interest.

III. A DECISION BY THIS COURT REQUIRING DISCLOSURE OF THE ASSIGNMENT PROVISION, UNLESS GIVEN ONLY PROSPECTIVE APPLICATION, WOULD CAUSE INJUSTICE AND HARDSHIP TO THE CONSUMER CREDIT INDUSTRY.

Ford Credit contends that this Court should reverse the decision below on the merits for the reasons stated in Parts

I and II of this brief. If, however, this Court were to affirm the decision below and to rule that the assignment provision must be disclosed as a security interest under the Act, then Ford Credit urges that such ruling be given only prospective application except as to the Buyers.

In appropriate circumstances, judicial decisions are given only prospective effect. The use of prospective relief has been endorsed by judges and commentators alike.[11] Prospective relief is granted to avoid the undue or unnecessary hardship of retroactive application of a decision. B. Cardozo, *The Nature of the Judicial Process,* 146-49 (1921). Through the use of prospective relief, a court is able to decide unresolved questions while maintaining stability and avoiding hardship. T. Fairchild, *supra,* 51 Marq. L. Rev. at 269-70.

The guidelines for determining when a ruling should be given prospective application in a civil action were set forth by this Court in *Chevron Oil Co.* v. *Huson,* 404 U.S. 97, 106-07 (1971):

> First, the decision to be applied nonretoactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied . . . or by deciding an issue of first impression whose resolution was not clearly foreshadowed . . . Second, it has been stressed that "we must . . . weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will

[11] T. Fairchild, *Limitation of New Judge—Made Law to Prospective Effect Only: "Prospective Overruling" or "Sunbursting",* 51 Marq. L. Rev. 254, 269-70 (1967-68); W. Schaefer, *The Control of "Sunbursts": Techniques of Prospective Overruling,* 42 NYU L. Rev. 631, 637 (1967); F. Beytagh, *Ten Years of Non-Retroactivity: A Critique and a Proposal,* 61 Va. L. Rev. 1557 (1975).

> further or retard its operation." . . . Finally, we have weighed the inequity imposed by retroactive application, for "[w]here a decision of this Court could produce substantial inequitable results if applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity." [Citations omitted.]

As discussed below, this case satisfies the *Chevron* guidelines for prospective relief.

A. An Adverse Decision On This Issue Was Not Clearly Foreshadowed.

The first *Chevron* guideline does not limit the doctrine of prospective relief to cases where the prior authorities were unanimous on the point at issue. Instead, this Court has given only prospective application to cases which decide an issue of first impression whose resolution was not "clearly foreshadowed." For example, in *Lemon* v. *Kurtzman,* 411 U.S. 192, 206-07 (1973), the Court was faced with the question of whether its decision that a state statute was unconstitutional should be applied retroactively. There had been disagreement over the validity of the statute beginning with the first decisions at the district court level and continuing up to this Court. The Court ruled that retroactive application was not appropriate since the issue it decided was one of first impression whose resolution was not clearly foreshadowed.

The Seventh Circuit refused to give only prospective application to the decision below on the ground that the weight of authority when the Contract was executed on September 30, 1977 was contrary to Ford Credit's interpretation of the Act. (J.A. 56). The Seventh Circuit is simply wrong in this analysis. As noted above, the case law is and has been sharply divided on this issue. Moreover, an examination of the cases decided prior to execution of the Con-

tract shows that Ford Credit's form of disclosure complied with the limited case law prevailing at that time.

During the first seven years that the Truth in Lending Act was in force, there were no reported decisions dealing with the assignment of unearned insurance premiums. As described above, there was no hint in the legislative history that this incidental interest was to be treated as a security interest under the Act. The Act and Regulation Z required disclosure of certain insurance information—but not information relating to unearned insurance premiums. Thus, Ford Credit and the entire consumer credit industry (*see* the brief filed herein by *amici curiae* Consumer Bankers Association, General Motors Acceptance Corporation and National Consumer Finance Association) relied on the Act, Regulation Z, the legislative history and the absence of any adverse decisions in continuing to disclose the assignment provision on the reverse side of installment contracts.

Three district court decisions were rendered on this issue before the September 30, 1977 date of the Contract in this case. No appellate decisions were rendered before that date. These district court decisions did not definitively resolve the issue or clearly foreshadow the result reached by the court below. These decisions certainly could not provide the basis for the industry to change immediately its standard contract forms. On balance, these decisions did not find fault with the industry-wide form of disclosure.

The first district court decision was *Edmondson* v. *Allen-Russell Ford, Inc.*, No. C75-940A (N.D. Ga. 1976) (Add. 18-26), *aff'd*, 577 F.2d 291 (5th Cir. 1978), *cert. denied*, 441 U.S. 951 (1979), in which the district court accepted Magistrate Cohen's recommendation and held that an assignment of unearned insurance premiums was a Truth in Lending Act security interest. However, after making an initial recom-

mendation in *Shanks* v. *Greenbriar Dodge, Inc.*, Civ. No. C75-1154A (N.D. Ga. 1976) (Add. 40-52), *rev'd*, 577 F.2d 296 (5th Cir. 1978), similar to his recommendation in *Edmondson*, Magistrate Cohen withdrew his recommendation and stated that he would not follow his previous ruling. (Add. 42). The district court in *Shanks* accepted the magistrate's revised position. Therefore, the prevailing precedent in the Northern District of Georgia in 1977 was the holding in *Shanks* that an assignment of unearned insurance premiums did not create a security interest requiring disclosure under the Truth in Lending Act.

The ruling in the third case on point, *Gennuso* v. *Commercial Bank and Trust Co.*, 425 F.Supp. 461 (W.D. Pa. 1976), also supported the position taken by Ford Credit and the credit industry generally. *Gennuso* held that even if an assignment of unearned insurance premiums were regarded as a security interest, it need not be specifically disclosed on the face of a credit contract. That decision was reversed by the Third Circuit *after* the instant contract was executed. 566 F.2d 437 (3d Cir. 1977).

The issue decided below was before the Seventh Circuit for the first time. (J.A. 56). That decision constituted a sharp break from the first two decisions on this issue by district courts in the Seventh Circuit—the decision in *Rounds* v. *Community National Bank*, 454 F.Supp. 883 (S.D. Ill. 1978), and the first opinion below (J.A. 9-18)—both of which held that an assignment of unearned insurance premiums was not a "security interest" requiring disclosure under the Act. These district court decisions are strong evidence that the limited judicial precedents available to the district courts (and the credit industry) as late as 1978 endorsed the form of disclosure made by Ford Credit here in 1977. When even the district courts sitting in the Seventh Circuit Court of Appeals failed in 1978 to predict correctly

how the Seventh Circuit would rule on the issue decided in its March 20, 1980 opinion, Ford Credit does not understand how that court could conclude that its decision was "clearly foreshadowed" (J.A. 56) at the time the Contract was executed in 1977.

The fact that the Circuit Courts of Appeals are split today with respect to contracts identical in all relevant respects supports Ford Credit's position that the law was and continues to be unclear on this issue. Moreover, the fact that the Federal Reserve Board staff has taken a position contrary to the Seventh Circuit's interpretation in the decision below emphasizes that the Seventh Circuit's position was not clearly foreshadowed.

B. Retroactive Application Would Not Further The Purpose Of The Act.

As noted above, the central purpose of the Act is to require uniform credit cost disclosures so that consumers can comparison shop for credit. 15 U.S.C. § 1601(a). Nowhere in the Seventh Circuit's lengthy opinion below was there any explanation of how its decision would further that purpose. The two expressly "reluctant" concurring opinions below by Judges Cudahy and Swygert noted in pertinent part that the court's holding would require "the prominent disclosure of a rather esoteric right" which if disclosed as a "security interest" merely "add[s] virtually inconsequential information—lengthening, complicating and trivializing the disclosure for no apparent benefit." (J.A. 63). While admitting that the violation of the Act found by it was "purely technical," the court below concluded that the credit industry should address its concern about the technical nature of certain requirements under the Act to Congress or to the Federal Reserve Board, not to the courts. (J.A. 50).

The credit industry has pursued the avenues suggested in the opinion below. As discussed above, the Federal Reserve staff recently issued Proposed Official Staff Interpretation FC-0173 under the present Act endorsing the form of disclosure used by Ford Credit and other consumer lenders. But, as noted above, the staff has deferred final action on the proposed interpretation pending the outcome of this case (Add. 58), thereby leaving the credit industry closer to the troubled waters of conflicting judicial decisions[12] than is proper, particularly in light of the clarity of the staff's position on the merits of this issue.

The credit industry expressed to the Congress its concern over the technical nature of certain requirements of the Act, as interpreted by the courts. By adopting the Simplification Act, Congress acted to "eliminate litigation based on purely technical violations of the Act." S. Rep. No. 96-73 at 17, [1980] U.S. Code Cong. & Ad. News at 892. But the Simplification Act will not become effective until April 1, 1982. 94 Stat. 185. Therefore, until the effective date of the Simplification Act or final action by the Federal Reserve staff, only this Court's hand, guided by the *Chevron* standard, can avoid the unfairly harsh result which would occur if an adverse decision by this Court—involving a purely technical and highly debatable claim under the Truth in Lending Act —were applied retroactively. Prospective application in this

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[12] By disclosing the assignment of unearned insurance premiums as a security interest at a time when the prevailing case law held that it was not, Ford Credit would have risked violating the Act by disclosing an over-inclusive security interest. " 'Describing a security interest where there is none' has been held to be 'additional and misleading information' " in violation of Regulation Z, 12 C.F.R. § 226.6(c). *Bartlett* v. *Commercial Federal Savings and Loan Association*, 433 F. Supp. 284, 287 (D. Neb. 1977).

case would be in accord with the intent of Congress as expressed in the Simplification Act.

Furthermore, retroactive application of such a decision would not result in more "meaningful disclosure" to consumers since conforming disclosure statements could only be given in future transactions. Retroactive application of unanticipated rulings would encourage lenders to make myriads of new disclosures in consumer contracts at the slightest shift in judicial currents, fearing that even the most strained reading of the Act today might tomorrow result in a holding of liability. Extensive additions to the disclosure statement will detract from really important information and will cause many borrowers not to read or understand the disclosure statement. The better solution is to apply prospectively any such technical decision in order to allow lenders time to add to their contracts only those provisions deemed necessary for the informed use of credit.

Prospective application of the statutory penalties would promote compliance with this Court's interpretation of the Act by penalizing any lender who does not revise his forms to comply with a clear pronouncement by the Court. Retroactive application of the decision cannot deter previous technical violations but will simply promote litigation against lenders who have in good faith attempted to comply with the Act and Regulation Z at a time when virtually the entire lending industry placed such assignment provisions on the back rather than the front of millions of installment contracts.

C. A Retroactive Decision Would Be Grossly Inequitable.

Although the dollar amount involved in this action is small, it would be misleading to ignore the staggering vol-

ume of transactions that are subject to the Act and the Regulation and to which the principles adopted in this case will apply. There are millions of consumer credit contracts outstanding in the United States today for automobile transactions alone representing more than $100 billion in consumer installment indebtedness.[13] Although these contracts vary significantly in their credit terms, they typically contain a reverse side disclosure of the assignment of unearned insurance premiums. This Court's decision will thus affect millions of consumer installment contracts subject to the Act and the Regulation. Retroactive application would simply provide windfall recoveries where there has been no injury, based on hyper-technical and ever-evolving constructions of the Act that threaten to disrupt established lending practices without furthering the goal of truth in lending.

The Truth in Lending area is particularly appropriate for prospective application of decisions. Many claimed violations of the Act (including the one alleged in this case) are highly technical and do not affect the borrower's understanding of the cost of credit or the terms of the loan. In *Sanders* v. *Auto Associates, Inc.*, 450 F. Supp. 900, 902 (D.S.C. 1978), Judge Chapman stated:

> Unfortunately, many of the truth in lending cases which have been instituted in this court have not been brought by plaintiffs who were misled or misinformed by the loan forms they attack. These plaintiffs have merely sought a windfall penalty from a lender by picking apart its loan form word by word in search of a technical deviation from the language of the statutes and regulations. The Truth in Lending Act was never

[13] According to the Board, consumer installment indebtedness outstanding in the United States for automobile transactions alone was $102,468,000,000 at year end 1978. 66 Federal Reserve Bulletin A40 (Table 1.56) (1980).

> meant to make the district courts forums for word games between lenders and borrowers in which a borrower's attorney who is adept at using legalese and arguing technicalities is awarded a prize for himself and his client. In order to avoid such misuse of the Truth in Lending Act, this Court will strongly construe its provisions against borrowers who were not misled by a lender's disclosure but merely seek a penalty for finding a technical problem with the loan form which could not have conceivably influenced his choice of credit.

There is ample precedent for granting prospective relief here. Long before the Act was adopted, the area of consumer lending was an area of prospective application of decisions. For example, in *Hare* v. *General Contract Purchase Corp.*, 249 S.W.2d 973 (Ark. 1952), a particular form of installment contract had been used in reliance on judicial interpretations of the state's constitutional limitation on interest rates. In the *Hare* decision, the court announced a new rule declaring the old form of contract invalid, but applied it only to future contracts.

Prospective relief has similarly been granted under the Act when form contracts are involved in order to avoid unfairly harsh impacts on lenders. In *McDaniel* v. *Fulton National Bank*, 571 F.2d 948 (5th Cir. 1978), the proper method of disclosure of an acceleration clause in the form contracts of three lenders was before the Fifth Circuit. In its decision, the *McDaniel* court found a violation of the Act respecting acceleration clause disclosure, but limited its ruling to transactions commencing 90 days after the date of the decision, except for the litigants in the case. Other courts have given only prospective application to decisions on the disclosure of security interests under the Act. *Ector* v. *Southern Discount Co.*, No. C78-899A (N.D. Ga. Sept. 15, 1980) (Add. 12-15) (only prospective application regarding failure to disclose assignment of homestead exemption as a security interest); *Sneed* v. *Beneficial Finance Co.*, 410

F.Supp. 1135, 1140-4 (D. Hawaii 1976) (only prospective application regarding disclosure of overinclusive security interest in after acquired property).

In short, the legislative history of the Act, a clearly reasonable interpretation of Regulation Z, and the case law prevailing when the Contract was executed all supported Ford Credit's form of disclosure. The purpose of the Act would not be advanced by giving retroactive application to an adverse ruling by this Court concerning the form of disclosure used by Ford Credit and virtually the entire consumer credit industry. It would be fundamentally unfair to impose potentially enormous penalties on the consumer credit industry for what is, at worst, a purely technical violation. If, in these circumstances, the Court rules against Ford Credit's position on the merits, such ruling should be given only prospective application except as to the Buyers.

CONCLUSION

For the reasons stated above, petitioners respectfully request the Court to reverse the judgment of the Court of Appeals below.

Respectfully submitted,

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ADDENDUM

ADDENDUM OF LEGAL AUTHORITIES

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Edmondson v. *Allen-Russell Ford, Inc.*, No. C75-940A (N.D. Ga. 1976)	Add. 18
James v. *Ford Motor Credit Company*, No. 78-1806 (10th Cir. 1980)	Add. 27
Shanks v. *Greenbriar Dodge, Inc.*, No. C75-1154A (N.D. Ga. 1976)	Add. 40
Souife v. *First National Bank of Commerce*, No. 78-2562 (5th Cir. Dec. 5, 1980) (order deferring consideration of petition for rehearing en banc)	Add. 53
Proposed Official Staff Interpretation FC-0173, 45 Fed. Reg. 63295 (Sept. 24, 1980)	Add. 54
Order suspending consideration of Proposed Official Staff Interpretation FC-0173, 45 Fed. Reg. 84074 (Dec. 22, 1980)	Add. 58

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF SOUTH CAROLINA
CHARLESTON DIVISION

ROSE MARY ANCRUM AND CHRISTOPHER ANCRUM, *Plaintiffs,* vs. CHARLESTON LINCOLN MERCURY, INC. AND FORD MOTOR CREDIT COMPANY, *Defendants.*	CIVIL ACTION NO. 78-804 ORDER OF SUMMARY JUDGMENT

This action was initiated by the Plaintiffs alleging four (4) violations by the Defendants of the Consumer Credit Protection Act, 15 USC § 1601 et seq. (commonly referred to as the Truth-In-Lending Act), and Regulation Z, 12 C.F.R. § 226.1 et. seq. stemming from a Consumer Credit transaction. The Plaintiffs seek statutory damages of One Thousand ($1,000) Dollars together with costs and attorney fees.

The Defendants answered the Complaint denying the material allegations. Additionaly, the Defendant, Ford Motor Credit Company, (hereinafter referred to as "Ford Credit") interposed a Counterclaim for the balance owed on the underlying debt.

Depositions were taken and are of record in these proceedings. Cross-Motions for Summary Judgment have been filed and oral argument upon the Motions has been heard.

On May 26, 1977 the Plaintiffs purchased a used 1975 Mercury, Comet automobile from Charleston Lincoln Mer-

cury, Inc. (hereinafter referred to as "Dealer") for the sum of Two Thousand Nine Hundred Forty-Seven and 12/100 ($2,947.12). In order to finance a portion of the purchase price, the Plaintiffs executed a South Carolina Retail Installment Contract. This Contract is a preprinted form prepared by the Defendant, Ford Credit. The terms of the transaction were entered onto the form and the form contract completed by the Dealer.

Ford Credit is a wholly owned subsidiary of Ford Motor Company. It provides the wholesale financing for the Dealer, commonly referred to as "floor planning". Ford Credit has provided a capital loan to the Defendant Dealer. Additionally 52% of the finance contracts resulting from sales of vehicles by the Dealer during 1977 and 1978 were assigned to Ford Motor Credit Company.

After the Plaintiffs executed the Retail Installment Contract, the Dealer executed the Contract as "Seller" through its Secretary-Treasurer under a provision which reads as follows:

> "The foregoing Contract hereby is accepted by the Seller and assigned to Ford Motor Credit Company in accordance with the terms of the assignment set forth on the reverse side hereof."

Thereafter, Ford Credit accepted assignment of the Contract, notified the Plaintiffs of the assignment and the Plaintiffs began making their payments to Ford Credit.

This Court has jurisdiction over the parties and the subject matter by virtue of 15 U.S.C. § 1640(e).

The Plaintiffs' first contend that the Contract fails to disclose a security interest taken by the Defendants in the proceeds of physical damage insurance and unearned or returned insurance premiums.

The Truth-In-Lending Act, 15 USC § 1638(a)(10), requires that the disclosure statement include the following:

> "[a] description of any security interest held or to be retained or acquired by the creditor in connection with the extension of credit and a clear identification of the property to which the security interest relates."

There is no definition of the term "Security Interest" or "Security" in the Act. However, the regulations promulgated under the Act 12 C.F.R. § 226.2(g) provide:

> " 'Security Interest' and 'Security' mean any interest in property which secures payment or performance of an obligation. The terms include but are not limited to, security interests under the Uniform Commercial Code, real property mortgages, deeds of trust and [various liens and a lease interest securing performance of an obligation]"

The Plaintiffs in this case contend that the provision for the assignment of unearned or returned insurance premiums and insurance proceeds from physical damage insurance, found in Paragraph 18 on the reverse side of the Contract form constitutes a security interest which is not disclosed on the face of the document. The front of the document contains the following description of the security interest taken:

> "Security Interest": Seller shall have a security interest under the Uniform Commercial Code in the property (described above) and in the proceeds thereof to secure the payment in cash of the Total of Payments and all other amounts due or to become due thereunder."

Paragraph 18 of the Contract is among the additional terms and conditions incorporated into the Contract by reference. Paragraph 18, found on the back of the Contract, reads as follows:

> "Buyer hereby assigns to Seller any monies payable under such insurance, by whomever obtained including returned or unearned premiums and Seller hereby is authorized on behalf of both Buyer and Seller to receive or collect same, . . . the proceeds from such insurance, by whomever obtained shall be applied toward replacement of the property or payment of the indebtedness hereunder in the sole discretion of the Seller."

There are three Circuit Court Decisions which have held that the failure to disclose the right to unearned and returned insurance premiums and proceeds of insurance, constitutes a violation of TILA, subjecting the Seller to liability. Two of these decisions involved the same written Contract as that which is before the Court in this Case. See *Edmondson* v. *Allen Russell Ford, Inc.* 5th Cir., 577 F.2d 291, Cert. denied, 441 U.S. 951; *Valencia* v. *Anderson Brothers Ford,* 7th Cir., F.2d ; and *Gennuso* v. *Commercial Bank and Trust Company,* (3rd Cir.) 566 F.2d, 437. These cases were all decided prior to the passage and approval by the President on March 31, 1980 of the "Truth-In-Lending Simplification and Reform Act" Title 6 of the "Monetary Control Act of 1980." P. L. 96-221, 94 Stat. 132.

Section 614(a) of the Truth-In-Lending Simplification and Reform Act amends 15 USC and § 1638 (a), which is the disclosure section of the Truth-In-Lending Act. Subsection (a)(9) of the Amendment reads as follows:

> "Where the credit is secured, [the creditor shall disclose to the extent applicable] a statement that a security interest has been taken in (a) the property which is purchased as part of the credit transaction, or (b) property not purchased as part of the credit transaction identified by item or type." U.S. Cong. & Adm. News, No. 3, May 1980, 94 Stat. 179.

The purpose of the Amendments to the original Act are clearly outlined in the Senate Report. S.R. 96-368, U.S.

Cong. & Adm. News, *supra*, p. 850, includes the following statement regarding the purpose of the 1980 Amendments:

> "Despite the act's clear successes, however, there is a growing belief among consumers and creditors alike that the act could be substantially improved. There is considerable evidence, for example, that disclosure forms given consumers are too lengthy and difficult to understand. Creditors, on the other hand have encountered increasing difficulty in keeping current with a steady stream of administrative interpretations and amendments, as well as highly technical judicial decisions. There is also evidence that many creditors have sincerely tried to comply with the act but, due to its increasing complexity and frequent changes, have nonetheless found themselves in violation and subject to litigation. In addition, this committee and other congressional and government sources have found the level of administrative enforcement by the Federal bank agencies seriously inadequate. In short, the committee believes that the interests of both consumers and creditors would be furthered by simplification and reform of the act."

The Senate Report addresses the specific amendment simplifying the security interest disclosure requirement, stating:

> "The security interest disclosure is also simplified to eliminate the technical disclosure of the type of security interest taken. When a security interest is being taken and property purchased as part of the credit transaction, this section requires a statement that a security interest has been or will be taken in the property purchased. When a security interest is being taken in property not purchased as part of the credit transaction, the committee intends this provision to require a listing by item or type of the property securing the transaction, but not a listing of related or incidental interests in the property. For example: a loan is secured by an automobile but would not require a listing of

> incidental or related rights which the property may have, such as insurance proceeds or unearned insurance premiums, rights arising under, or waived in accordance with State Law, accessions, accessories or proceeds." U.S. Cong. & Adm. News, *supra,* page 864.

Following the passage of the "Truth-In-Lending Simplification and Reform Act," the 10th Circuit Court of Appeals addressed this issue in the case of *James* v. *Ford Motor Credit Co.*, et. al., ____ F.2d ____ (decided June 24, 1980) (D.C. No. Civ. 78-F-647). The Court affirmed the lower court holding that the provision for the assignment of physical damage insurance proceeds and unearned or returned premiums did not constitute a security interest required to be disclosed under the Act. In so doing, the Court considered the Legislative history of the 1980 Amendments to the Truth-In-Lending Act to help in discerning Congressional intent.

In conjunction with the 1980 Amendments and their Legislative history, the Court further considered the recent decision of the United States Supreme Court, found in *Ford Motor Credit Co.* v. *Milhollin,* ____ U.S. ____ 48 L.W. 4145, decided February 20, 1980. In that decision the Court stated:

> "The concept of 'meaningful disclosure' that animates TILA (citation omitted), cannot be applied in the abstract. *Meaningful* disclosure does not mean *more* disclosure. Rather, it describes a balance between 'competing considerations of complete disclosure . . . and the need to avoid . . . 'information overload' (citations omitted) and striking the appropriate balance is an empirical process that entails investigation into consumer psychology and that presupposes broad experience with credit practices." (Emphasis in original).

Analogizing the statement of the Supreme Court in *Milhollin* to the 1980 Amendments and their legislative history, the *James* Court reasoned:

> "The *Milhollin* approach parallels the intent of Congress in enacting the 1980 Amendments and the legislative history of those Amendments. The effort is to strengthen the impact of TILA by simple, concise disclosures which can be understood by consumers and creditors." *James* v. *Ford Motor Credit Co., supra,* p. 9.

Applying this reasoning, the Court concluded:

> "We are convinced that the Act does not require and Congress did not intend it to require, an exemplification of that interest on the face of the installment contract . . .
>
> "The application of *Milhollin* and the 1980 actions of Congress present no retroactivity problem. We are concerned only with civil liability for nondisclosure. The buyers have shown no damage. Our decision establishes no new principle of law. Rather, it recognizes the Congressional intent. Application to this case furthers the operation of TILA and produces an equitable result. See *Chevron Oil Co.* v. *Huson,* 404 U.S. 97, 106-107.

The inclusion of the assignment of unearned or returned insurance premiums and insurance proceeds would provide the consumer with "informational overload". Conversely, the *James* decision, *supra,* strikes a ". . . balance between 'competing considerations' of complete disclosure . . . and the need to avoid 'informational overload'." *Ford Motor Credit Co.* v. *Milhollin, supra,* 48 L.W. at 4149. The decision recognizes and enhances the intent of Congress to provide the consumer with a meaningful, non-technical, simple and concise disclosure. I therefore conclude that the assignment of insurance proceeds and unearned or returned insurance premiums do [sic] not constitute a security interest which is required to be disclosed on the face of the contract.

The Plaintiffs secondly contend that the Defendant, Ford Credit was a "creditor", within the purview of the Act, and

should have been disclosed as such on the face of the Contract. The Plaintiffs argue that the failure to label Ford Credit as such is a violation. In support of this position, Plaintiffs point out the continuing business relationship existing between the Defendants.

It is the conclusion of this Court that Ford Credit is properly identified on the Contract. There is no labeling requirement. *Sadie Morris* vs. *Kate McLaurin Company and General Electric Credit Company* D.C.S.C., Civ. Act File No. 76-2407, July 8, 1978 aff'd USC 4th Cir. 78-1605, June 20, 1978.

Ford Credit is named on the face of the Contract in the provision found next to the designated place for the signature of the Buyer, in the provision which purports to assign the Contract to it from the Dealer. The provision reads as follows:

> "The foregoing Contract hereby is accepted by the Seller and assigned to Ford Motor Credit Company in accordance with the terms of the assignment set forth on the reverse side hereof."

The Contract properly identifies Ford Motor Credit Company in accordance with the requirements of the Act. *Augusta* v. *Marshall Motor Company, and Ford Motor Credit Company,* 453 F.Supp. 912 (D.C., Ohio), 1977; *Main* v. *Faller Ford,* et. al., Civ. No. 74-337, (W.D. Pa. April 22, 1976); *Milhollin* v. *Ford Motor Credit Company,* 588 F. 2d 753 (9th Cir. 1978).

Next the Plaintiffs argue that the failure to itemize the license, title and registration fee constitutes a violation of the Act. Regulation Z, 12 C.F.R. § 226.4 (b), lists types of charges which do not have to be included in the finance charge as long as they are itemized and disclosed to the consumer with the heading "other charges". Section

226.4 (b) itemizes the various charges, and subsection (4) reads "License, Certificate of Title and Registration Fees imposed by law".

The Federal Reserve Board issued its Staff Opinion on October 14, 1977 addressing this specific issue. See CCH § 31,724 (Consumer Credit Guide, Transfer Binder). That opinion states in applicable part as follows:

> "Staff is of the opinion that the three components within § 226.4 (b) (4) need not be separately itemized, if a creditor discloses the total fee comprising the three components and indicates the types of fees included within that total such fee qualifies for exclusion from the finance charge"

This Court has accorded substantial weight to the opinion of the Federal Reserve Board. See *Moore* v. *Great Western Savings and Loan Ass'n*, 513 F.2d 688, 690 (9th Cir., 1975); *Eby* v. *Reb Realty, Inc.*, 495 F.2d 646, 650 (9th Cir. 1974); *Bohn* v. *Hibernia Bank*, 493 F.Supp. 135 (9th Cir. 1974); *Taylor* v. *R. H. Macy and Co., Inc.*, 481 F.2d 178, 180 (9th Cir. 1973); *Douglas* v. *Beneficial Finance Company*, 468 F.2d 453, 456 n.2 (9th Cir. 1972); and *Mourning* v. *Family Publications Service*, 411 U.S. 356, 365 (1973).

There is no logical explanation for categorizing "License, Certificate of Title, and Registration Fees imposed by law "as one element to be disclosed if the authors of Regulation Z had intended for each component to be separately stated. The Regulation speaks for itself in this regard. *R. L. Knighten* v. *Century Dodge, Inc.*, Civ. No. 77-26 Mac. (M.D. Ga., 1978). Therefore, I conclude that the disclosure requirements of the Act and Regulation have been met, and their is no violation.

Finally the Plaintiffs contend that the handwritten addition on the Contract for a ". . . Doc Fee $25" which appears

next to the printed category heading "other charges", violates the Act and Regulation because it is not clear, conspicious and meaningful. The documentary fee is properly grouped with other charges. § 226.6(a) of Regulation Z specifically allows handwritten disclosures. The fee is legibly written. Finally, there is no requirement in the Act or Regulation that an added charge such as this be more conspicuous than other terms. This contention is without merit.

I have considered in detail each allegation of the Plaintiffs and find no violation of the Truth in Lending Act. Having disposed of these issues, the remaining issues concern the Counterclaim of the Defendant Ford Credit. I conclude that the Counterclaim is permissive and not compulsory. *Williams* v. *Beneficial Finance Company of Fayetteville, Inc.*, 599 F.2d 1322 (4th Cir., 1979). There is no independent jurisdictional basis for the counterclaim and it must, therefore, be dismissed. Therefore, it is

ORDERED that the Counterclaim of the Defendant, Ford Credit, be dismissed;

ORDERED that Judgment be entered for the Defendants dismissing the Complaint.

IT IS SO ORDERED.

/s/ FALION B. HAWKINS
Judge, United States District Court

Charleston, SC
August 18, 1980

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

GENEVA ECTOR, *Plaintiff,* vs. SOUTHERN DISCOUNT COMPANY, *Defendant.*	CIVIL ACTION NO. C78 899A

EXCERPTS FROM SEPTEMBER 15, 1980 ORDER OF COURT AT 1, 15-20

ORDER OF COURT

Presently before the Court are the report and recommendation of United States Magistrate J. Owen Forrester and the parties' responses thereto. The magistrate recommends that the plaintiff's motion for summary judgment be denied. Although several difficult issues are presented, the Court APPROVES the recommendation that plaintiff's motion for summary judgment be DENIED and ADOPTS it as the order of the Court. The facts pertinent to each issue are set forth in connection with the individual discussion of the issue to which they pertain.

I. DISCLOSURE OF GEORGIA LOAN FEES IN CONNECTION WITH COMPUTATION OF PREPAID FINANCE CHARGE

• • • •

II. FAILURE TO DISCLOSE SECURITY INTEREST IN HOMESTEAD EXEMPTION

Plaintiff also complains of defendant's failure to disclose as a security interest on the front of the disclosure form the plaintiff's assignment of her homestead exemption. Defendant does not object to the magistrate's conclusion that this failure constitutes a violation under *Elzea* v. *National Bank of Georgia,* 570 F.2d 1248 (5th Cir. 1978). Plaintiff objects, however, to the further conclusion that defendant is entitled to a defense under 15 U.S.C. § 1640(f) (quoted *supra* p. 14). Defendant contends, relying upon the affidavit of its Senior Vice President, that it drafted its disclosure according to the interpretation given Regulation Z, 12 C.F.R. § 226.2(gg), by this Court in *Mims* v. *Dixie Finance Corp.,* 426 F.Supp. 627 (N.D. Ga. 1976) (*en banc*). *Mims* was in effect overruled by *Elzea.*

As did Judge Freeman in *Hamilton* v. *Southern Discount Co.,* No. 79-27A (N.D. Ga. May 30, 1980), the undersigned declines to rule upon the question whether section 1640(f) comprehends judicial interpretations of Regulation Z. *But see* note 7, *infra.* Instead, the Court concurs in the conclusion reached by Judge Freeman in *Hamilton* that *Elzea* should be given only prospective application. In light of the recent Fifth Circuit decision in *Travis* v. *Trust Company Bank,* Nos. 78-2812, 78-2890 (5th Cir. July 9, 1980), the endorsement of Judge Freeman's decision must be qualified as explained below. Judge Murphy has reached the same conclusion as did the *Travis* court in *Brown* v. *Termplan,* 459 F.Supp. 160 (N.D. Ga. 1978).

The Supreme Court has set forth a three-part inquiry for determining whether a given judicial decision ought to be applied retroactively:

> In our cases dealing with the nonretroactivity question, we have generally considered three separate fac-

> tors. First, the decision to be applied nonretroactively must establish a new principle of law, either by overruling clear past precedent on which litigants may have relied, *see e.g., Hanover Shoe, Inc.* v. *United Shoe Machinery Corp.*, [392 U.S. 481, 496], or by deciding an issue of first impression whose resolution was not clearly foreshadowed, *see, e.g., Allen* v. *State Board of Corrections,* [392 U.S. 544, 572]. Second, it has been stressed that "we must * * * weigh the merits and demerits in each case by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." *Linkletter* v. *Walker,* [351 U.S. 618, 629]. Finally, we have weighed the inequity imposed by retroactive application, for "[w]here a decision of this Court could produce substantial inequitable results of [sic] applied retroactively, there is ample basis in our cases for avoiding the 'injustice or hardship' by a holding of nonretroactivity." *Cipriano* v. *City of Houma,* [395 U.S. 701, 706].

Chevron Oil Co. v. *Huson,* 404 U.S. 97, 106-07 (1971).

In *Travis* and in *Brown,* the courts began their discussions by noting that the transactions involved ante-dated this Court's opinion in *Mims* and that as a result the lender could not have relied on *Mims. Travis,* slip op. at p. 7108; *Brown,* 459 F.Supp. 160, 162. The *Travis* court also went on to conclude that the [sic] in *Elzea* should have been anticipated by "reasonable, prudent creditors." Slip. op. at 7108. In the instant case the transaction at issue post-dated *Mims,* and the defendant undisputedly relied upon *Mims.* Thus *Elzea* "establish[ed] a new principle of law . . . by overruling clear past precedent on which litigants may have relied. . . ." *Chevron,* 404 U.S. 97, 106. Indeed, defendant not only "may have relied" but did in fact rely upon *Mims.* As a result of this actual reliance, the Court need not be concerned with *Travis'* discussion of the foreseeability of the *Elzea decision.* In any event such foreseeability must

be viewed in light of defendant's undisputed actual reliance upon *Mims*.

In answering the second *Chevron* inquiry, the *Travis* court emphasized that the Truth in Lending Act is designed to deter disclosure violations and not merely to compensate actual injuries. The purpose of the Act and the private enforcement scheme adopted by Congress would "be better served by having *Elzea* apply retroactively." Slip. op. at 7108. In this case retroactive application of *Elzea* would not meaningfully deter this defendant or others from disclosure violations. With respect to the sort of disclosure now required by *Elzea*, the defendant conformed its disclosure to the then-current state of the law as expressed in this Court's *en banc* decision in *Mims*. Thus, the defendant having done all that was then required by law, the retroactive application of *Elzea* to this transaction would be an example of the strictest, most absolute liability without fault. Such liability is required by neither the purpose nor express language of the Truth in Lending Act.

"The third test of *Chevron* is whether inequitable results would arise if the *Elzea* holding is applied retroactively." *Travis*, slip op. at 7109. The *Travis* court noted that the defendant lender in that case had changed its consumer lending forms early in 1976 and that as a result, the one-year statute of limitations in 15 U.S.C. § 1640 made it unlikely that the defendant would suffer great exposure. There are no facts before this Court indicating the potential exposure of Southern Discount on loan contracts similar to the one at issue here. This Court nevertheless believes that an inequitable result would arise from the imposition of *any* liability upon this defendant after its undisputed, good faith, actual reliance upon an *en banc* decision of this Court.

Thus, with respect of each of the inquiries mandated by *Chevron,* this Court believes the undisputed good faith, actual reliance of the defendant on the *en banc* decision in *Mims* to be significant grounds for distinguishing this case from the *Travis* case. Thus, the Court will not apply *Elzea* retroactively to transactions in which the lender undisputedly actually relied upon *Mims.*[7]

III. FAILURE TO DISCLOSE ALLEGED SECURITY INTEREST IN PROCEEDS OF INSURANCE

Plaintiff also complains that defendant failed to disclose the following language on the front of the disclosure as a security interest:

> Borrower will keep the collateral (which shall be at Borrower's risk), insured for a reasonable amount against loss by fire or theft (also accidental physical damage on motor vehicles). The proceeds of property insurance shall be payable to both Lender and Borrower as their interests may appear; and Lender may apply insurance proceeds paid to it at its option to repair property or to the debt.

This district has held previously that such an assignment of insurance proceeds need not be disclosed as a security interest. *E.g., Bohanan* v. *Southern Discount Co.,* C79-255A (N.D. Ga. July 30, 1980) (Freeman, J.); *Hardy* v. *Southern Discount Co.,* C79-1052A (N.D. Ga. July 23, 1980) (Shoob,

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[7] Although the Court need not decide the precise question of the applicability of 15 U.S.C. § 1640(f), obviously the above discussion has much the same effect as applying 1640(f). In defining the issue before it, the *Travis* court suggested a close relationship between the good faith reliance issue and the retroactivity issue when it stated that "Appellant contends that the civil liability provisions of TILA do not apply when there is good faith reliance upon case law, and therefore, that *Elzea* should be applied prospectively only." Slip op. at 7107.

J.); *Bolden* v. *Maryville Loan and Finance Corp.*, No. C76-130A (N.D. Ga. 1977) (Freeman, J.) *appeal docketed* No. C78-1050 (5th Cir. Jan. 6, 1978); *Bolden* v. *Legal Securities, Inc.*, No. C76-845A (N.D. Ga. 1977) (Henderson, J.); *Jones* v. *State Loan and Thrift Corp.*, No. C75-2148A (N.D. Ga. 1977) (Edenfield, J.). Recent Fifth Circuit cases have construed the term "security interest" somewhat broadly. *E.g., Edmondson* v. *Allen-Russell Ford, Inc.*, 577 F.2d 291 (5th Cir. 1978); *Elzea, supra.*

The undersigned believes that in technical areas of the law, uniformity of decisions is often desirable. This is especially so in truth in lending, where a good faith attempt by a lender to satisfy one decision-maker could cause the lender to run afoul of the dictates of another decision-maker. The Act's purpose of enhancing meaningful disclosure so that borrowers may intelligently shop for credit is promoted when all lenders are attempting to follow the same legal authority. But where lender A drafts notes according to a decision of Judge X and lender B drafts notes according to a differing decision of Judge Y, the lending community's resulting confusion will be reflected in confusing disclosures of credit information. Both lenders and borrowers are thus best served by a single, rational line of legal authority governing truth in lending disclosure. That line of authority may not always be absolutely correct, but it is, of course, correctable by appeal. In that regard, the Court notes that one of the cases cited above is already on appeal and was argued in December, 1979. Until such time as the Fifth Circuit rules, this Court will adhere to the precedent of *Bolden*, *Bolden*, and *Jones*.

Thus, for the reasons set forth in this part of the order, the Court finds no violation in defendant's failure to disclose the assignment of insurance proceeds as a security

interest, and for all the reasons set forth above the Court APPROVES and ADOPTS as the order of this Court the magistrate's recommendation that the plaintiff's motion for summary judgment be DENIED. Although defendant has not moved for summary judgment, this order would appear to dispose of the case. Accordingly, plaintiff may show cause within ten (10) days why judgment should not be entered for defendant.

SO ORDERED, this 15 day of Sept., 1980.

/s/ Charles A. Moye, Jr.
UNITED STATES DISTRICT JUDGE

RECOMMENDATION OF SPECIAL MASTER
APRIL 29, 1976

IN THE
UNITED STATES DISTRICT COURT
For the Northern District of Georgia
Atlanta Division

CATHERINE EDMONDSON,
Plaintiff,

vs.

ALLEN-RUSSELL FORD, INC. and FORD MOTOR CREDIT COMPANY,
Defendants.

CIVIL ACTION
NO. C75-940A

RECOMMENDATION OF SPECIAL MASTER

Before the Court is an earlier recommendation of the dismissal of Allen-Russell Ford, Inc. pursuant to settlement agreement. Also before the Court are motions for summary judgment by plaintiff and defendant Ford Motor Credit Company.

Plaintiff's first contention centers on the undisclosed acceleration clause. That clause provides that on default, "Seller shall have the right to declare all amounts due or to become due hereunder to be immediately due and payable." This is clearly an undisclosed default charge. *Whitehead* v. *Harry White Ford,* C75-695A (Freeman, J. 1976).

Plaintiff's second contention is that the defendant violated the Act by failing to itemize the finance charge even though the finance charge is composed of only a single element. In the case of a credit sale of goods, such as in the

case at bar, that single element is called time price differential. In the case of a loan, that single element is called interest.

With respect to both credit sales and credit loans, Regulation Z requires disclosure of "the total amount of the finance charge with description of each amount included, using the term finance charge." Regulation Z § 226.8(c)(8) and (d)(3). This is not the clearest language. It does not appear to contemplate the single-element finance charge. It is at least ambiguous as to whether the finance charge must have a dual label when composed of a single element.

Very early in the history of truth in lending, in 1969, a pamphlet was published entitled *What You Ought to Know about Truth in Lending*. The pamphlet stated: "Material in this pamphlet has been prepared by the Board of Governors of the Federal Reserve System." Attached are relevant portions of that pamphlet. The Board gave very clear examples in Exhibits A, B, C and D, that where the finance charge contained a single element, the label "finance charge" alone should be used to describe that element. This pamphlet was issued before any contrary court decisions.

It is true that the pamphlet should not be totally relied upon as a substitute for the regulation, for business transactions and state law vary. But no such variation could affect the accuracy of the portrayal of the single label "Finance Charge."

Furthermore, in staff position letter No. 682, dated April 25, 1973, it was stated that only the single label "Finance Charge" was to be given to the single element finance charge and that to give a dual label could obscure the clear impact of the disclosure of finance charge and therefore be misleading and confusing. Attached hereto is a copy of that letter.

This district has never spoken on the issue of whether the single element finance charge should be given a dual label. But it has approved many disclosure statements where only the single label was given to the single element finance charge.

There is in this district one recommendation which treated the point. In *Paer* v. *First National Bank of Tucker*, C74-1402A, as a second reason for holding for the plaintiff, the Special Master noted that authority in other districts and staff letters required itemization of the finance charge even though composed of a single element, interest. The Special Master was correct in his citations of authority from other districts, but he did not cite staff position letter No. 682. In any event, that recommendation did not become precedent. Judge Freeman entered judgment on the recommendations because they were unopposed.

This Special Master notes the alternate holdings clearly supporting plaintiff's contentions in *Ives* v. *W. T. Grant Company*, 522 F.2d 749 (2nd Cir. 1975); *Ljepava* v. *M.L.S.C. Properties, Inc.*, 511 F.2d 935 (9th Cir. 1975); *Johnson* v. *Associates Finance, Inc.*, 369 F.Supp. 1121 (S.D. Ill. 1974); *Myers* v. *Clearview Dodge Sales, Inc.*, 384 F.Supp. 722 (E.D. La. 1974). This Special Master also notes that each of these decisions rules contrary to the law of this District on other points.

About four months after the decision in *Ives* v. *W. T. Grant, supra*, the Board of Governors promulgated an interpretive ruling that there is no need for description or identification where the finance charge is composed of a single element. Attached hereto is a copy of that ruling.

Now this Special Master does not recommend giving weight to letters written by Federal Reserve Board staff employees criticizing court decisions. *Willis* v. *Town*

Finance Corp. of Atlanta, C74-1489A (Moye, J.). But this Special Master thinks courts should be reluctant to declare that settled and consistent interpretations of the Board are erroneous. *Philbeck* v. *Timmers Chevrolet Company,* 499 F. 2d 971 (5th Cir. 1974).

Plaintiff contends that the Board's Interpretive Ruling is plain wrong. Plaintiff goes to the Act itself and cites 15 USC 1638(a)(6). That section provides that a creditor must disclose:

> . . . the amount of the finance charge, which may in whole or in part be designated as a time price differential or any similar term to the extent applicable.

With the permissive "may" this section certainly does not stand unambiguously in support of plaintiff's contention.

Plaintiff argues that legislative history of the Truth in Lending Act supports his contentions. But to the Special Master, the Regulations and interpretations of the Board are much more important in fixing the meaning of the Act. The Act delegates to the Board the power to make regulations containing:

> . . . such classifications, differentiations, or other provisions, and may provide for such adjustment and exceptions for any class of transactions as in the judgment of the Board are necessary or proper to effectuate the purposes of this subchapter, to prevent circumvention or evasion thereof, or to facilitate compliance therewith. 15 USC 1604.

The Act also provides:

> Regulations of the Board need not require that disclosures pursuant to this part be made in the order set forth in this part, and may permit the use of terminology different from that employed in this part if it conveys substantially the same meaning. 15 USC 1632.

As Judge Edenfield noted in *Roberts* v. *National School of Radio & Television Broadcasting*, 374 F.Supp. 1266, 1269 (N.D. Ga. 1974)

> The Supreme Court has only recently observed that the authority and expertise which the Federal Reserve Board exerts in developing the enforcement provisions of the TIL is nearly absolute *Mourning* v. *Family Publications Service, Inc.*, 411 U.S. 356, . . . (1973).

Since the Board has stated its interpretation first and since this District Court has not held to the contrary, this Special Master concludes that the single label, "Finance Charge," is sufficient where the finance charge contains only a single element.

Plaintiff's third contention is that defendant failed to disclose its security interest in insurance proceeds, unearned insurance premiums, and personalty left in the car after repossession. Regulation Z § 226.8(b)(5) requires a clear identification of the property to which the security interest relates. The disclosed clause shows a security interest in the car "and in the proceeds thereof." The undisclosed clause dealing with property damage insurance to be obtained by Buyer for the protection of the interest of buyer and seller, reads:

> Buyer hereby assigns to Seller any monies payable under such insurance, by whomever obtained, including returned or unearned premiums, and Seller hereby is authorized on behalf of both Buyer and Seller to receive or collect same, to endorse checks or drafts in payment thereof, to cancel such insurance or to release and settle any claim with respect thereto. The proceeds from such insurance, by whomever obtained, shall be applied toward replacement of the property or payment of the indebtedness hereunder in the sole discretion of seller.

First, let us deal with insurance proceeds in case of damage to the car. The question is whether those insurance proceeds are encompassed in the disclosed security interest in the car "and in the proceeds thereof." This Special Master concludes that proceeds from the involuntary, as well as the voluntary, disposition of the car are encompassed. Ga. Code Ann. § 109A-9-306; *PPG Industries, Inc.* v. *Hartford Fire Insurance Co.*, 384 F. Supp. 91 (S.D. N.Y. 1974); *Fireman's Fund American Ins. Co.* v. *Ken-Lori Knits, Inc.*, 399 F. Supp. 286 (E.D. N.Y. 1975). The equation of voluntary and involuntary disposition is ancient in the law. This is revealed in the well-known history of the relationship between the common law actions of trover and conversion on the one hand and assumpsit on the other. Where property was tortiously disposed of, the injured party could presume that the wrongdoer had promised to buy it. Thus, the injured party could waive the tort and sue assumpsit.

The next question is whether the defendant took a security interest in returned and unearned premiums for property damage insurance. The undisclosed clause states the buyer's interest is assigned. The last sentence of that clause speaks of use of the insurance proceeds to pay the debt. In the contract, insurance proceeds appear to include returned and unearned premiums. Thus, there is an assigned for purpose of security.

Now, the question is whether returned or unearned premiums from property damage insurance are included in the disclosed security interest in the car "and the proceeds thereof." There is no precedent known to the Special Master on this point. This Special Master concludes that those premiums are not included in that disclosed security interest. Those premiums might be proceeds of the insurance policy, but they are not proceeds of the car.

Thus, the defendant has failed to disclose its security interest in returned and unearned premiums of property damage insurance. The next question is whether this violation is so minimal that it should be disregarded. The answer is no. If the security interest was important enough for defendant to acquire, it was important enough to disclose.

With regard to personal property, an undisclosed clause of the contract provides:

> Any personalty in or attached to the Property when repossessed may be held by Seller without liability and buyer shall be deemed to have waived any claim thereto unless written demand by certified mail is made upon Seller within 24 hours after repossession.

This clause is not a part of any clause dealing with indebtedness. It does not create a security interest in the personalty to secure payment of the debt.

WHEREFORE, it is recommended that plaintiff's motion for summary judgment be granted and that plaintiff have judgment in the amount of $1,000 plus reasonable attorneys fees.

Plaintiff's attorney is directed to submit within ten days an affidavit of legal services.

This 29th day of April, 1976.

/s/ Ezra H. Cohen
Ezra H. Cohen
BANKRUPTCY JUDGE,
Sitting as Special Master

(Note: Exhibits omitted in printing.)

ORDER OF THE DISTRICT COURT
AUGUST 27, 1976

IN THE
UNITED STATES DISTRICT COURT
Northern District of Georgia
Atlanta Division

CATHERINE EDMONDSON,
Plaintiff,

vs.

ALLEN-RUSSELL FORD, INC. and FORD MOTOR CREDIT COMPANY,
Defendants.

CIVIL ACTION
NO. C75-940A

ORDER

This truth in lending action is before this court for review of the special master's recommendation of April 29, awarding judgment in favor of the plaintiff in the amount of $1,000 against defendant Ford Motor Credit Co. and of his recommendation of May 14, awarding the plaintiff $900 in reasonable attorney's fees. Also before this court is the master's recommended dismissal of the complaint as it relates to Allen-Russell Ford, Inc.

Upon review of the record, the court finds itself in agreement with the special master's conclusion that the defendant failed to disclose the fact that it asserted a security interest in returned or unearned premiums of the automobile insurance. Such a failure to dissolve is a violation of 12 C.F.R. 226.8(b)(5). The court therefore ADOPTS the special master's recommendation on this issue and AWARDS the plaintiff judgment in the amount of $1,000 and $900 in reasonable attorney's fees against de-

fendant Ford Motor Credit Company and DISMISSES the complaint as it relates to defendant Allen-Russell Ford, Inc.

So ORDERED, this 27th day of August, 1976.

/s/ NEWELL EDENFIELD
NEWELL EDENFIELD
United States District Judge

OPINION OF THE COURT OF APPEALS FOR THE TENTH CIRCUIT JUNE 24, 1980

UNITED STATES COURT OF APPEALS TENTH CIRCUIT

No. 78-1806

JODY JAMES AND BARBARA JAMES,

Plaintiffs-Appellants,

v

FORD MOTOR CREDIT COMPANY AND DEL NORTE MOTOR COMPANY,

Defendants-Appellees.

Appeal from the United States District Court for the District of Colorado (D. C. No. Civ. 78-F-647)

Richard J. Rubin (with him on the briefs were Paul L. Biderman and Timothy Meehan, attorneys for Northern New Mexico Legal Services, Inc. and Le Roy Cordova) for appellants.

Lawrence W. Treece (with him on the briefs were Holme, Roberts and Owen, and Richard L. Schrepferman and Jeffrey A. Chase) for appellees.

Before SETH, Chief Judge, BREITENSTEIN and DOYLE, Circuit Judges.

BREITENSTEIN, Circuit Judge.

This action, which arose in Colorado, seeks recovery of a statutory civil liability for failure to disclose in an automobile installment purchase contract the right of the seller to a returned and unearned insurance premium on a policy

covering physical damage insurance. The claim is made under the Truth in Lending Act, TILA, 15 U.S.C. § 1601 et seq. as implemented by Federal Reserve Board Regulation Z, 12 C.F.R. § 226. The district court granted a motion to dismiss and the plaintiffs-buyers appeal. We affirm.

The plaintiffs-appellants, Jody and Barbara James, purchased a pick-up truck from defendant-appellee Del Norte Motor Company and executed an installment purchase contract which was assigned to Ford Motor Credit Corporation. The contract shows a cash price of $5395.00, down payments of cash and trade-in totalling $900.50, and a balance due of $4,494.50. To this are added other charges consisting of $359.84 for insurance and $5.50 registration fee. Also added is a finance charge of $1,238.92, at an annual interest rate of 15.40%. The balance due is payable in monthly installments of $169.41.

Paragraph 13 of the signed face page of the contract reads:

> "Security Interest: Seller shall have a security interest under the Uniform Commercial Code in the Property (described above) and to the proceeds thereof to secure the payment in cash of the Total of Payments and all other amounts due or to become due thereunder."

Paragraph 15 on the face page provides that the terms and conditions on the reverse side are incorporated by reference. Paragraph 18 on the reverse side relates to insurance and among other things provides:

> "Buyer hereby assigns to Seller any monies payable under such insurance, by whomever obtained, including returned or unearned premiums, and Seller hereby is authorized on behalf of both Buyer and Seller to receive or collect same, * * *. The proceeds from such insurance, by whomever obtained, shall be applied toward replacement of the indebtedness hereunder in the sole discretion of the Seller."

TILA requires, 15 U.S.C. § 1631(a), that a creditor "clearly and conspicuously, in accordance with the regulations of the Board" disclose the information mandated by the Act. Reg. Z, 12 C.F.R. § 226.8(a) provides that all the disclosures be made on either:

> "(1) The note or other instrument evidencing the obligation on the same side of the page and above the place for the customer's signature; or
>
> (2) One side of a separate statement which identifies the transaction."

Failure to disclose properly the required information subjects the offender to a civil liability of not more than $1,000.00 plus reasonable attorneys' fees. 15 U.S.C. § 1640(a). The purchasers sue for the statutory liability and attorneys' fees. The trial court held that the assignment of the returned and unearned portion of the insurance premium was not a security interest under the Colorado version of the Uniform Commercial Code. See Colo. Rev. Stat. (1973) § 4-9-102.

TILA requires, 15 U.S.C. § 1638(a)(10), the disclosure of "[a] description of any security interest held or to be retained or acquired by the creditor in connection with the extension of credit, and a clear identification of the property to which the security interest relates." The Act does not define "security" or "security interest." Reg. Z provides, 12 C.F.R. § 226.2(gg):

> " 'Security interest' and 'security' mean any interest in property which secures payment or performance of an obligation. The terms include, but are not limited to, security interests under the Uniform Commercial Code, real property mortgages, deeds of trust and [various liens and a lease interest securing performance of an obligation]."

The reference to the Uniform Commercial Code specifically declares that it is not a limitation. Although the interplay of federal and state law presents problems, the right to the TILA civil liability for nondisclosure rests on federal law. TILA is remedial legislation, designed to prevent predatory creditor practices, and must be liberally construed to effectuate the intent of Congress. See Mourning v. Family Publications Service, Inc., 411 U.S. 356, 365, and Littlefield v. Walt Flanagan and Company, 10 Cir., 498 F.2d 1133, 1136.

Three circuits have held that nondisclosure of the seller's rights to unearned and returned premiums violates TILA and subjects the seller to the statutory liability. See Gennuso v. Commercial Bank & Trust Company, 3 Cir., 566 F.2d 437; Edmondson v. Allen-Russell Ford, Inc., 5 Cir., 577 F.2d 291, cert. denied 441 U.S. 951; and Valencia v. Anderson Brothers Ford, 7 Cir., —— F.2d ——. The last of these, Valencia, was decided on March 20, 1980.

On March 31, 1980, the President approved the "Truth in Lending Simplification and Reform Act" as Title VI of the "Monetary Control Act of 1980." P.L. 96-221, 94 Stat. 132. Section 614(a) amends 15 U.S.C. § 1638(a), the disclosure section of TILA. Subsection (a)(9) reads, U.S. Cong. & Adm. News, No. 3, May 1980, 94 Stat. 179:

> "Where the credit is secured, [the creditor shall disclose to the extent applicable] a statement that a security interest has been taken in (A) the property which is purchased as part of the credit transaction, or (B) property not purchased as part of the credit transaction identified by item or type."

S. R. 96-368, U.S. Cong. & Adm. News, supra, p. 850, states the purpose of the 1980 amendments thus:

> "Despite the act's clear successes, however, there is a growing belief among consumers and creditors alike

that the act could be substantially improved. There is considerable evidence, for example, that disclosure forms given consumers are too lengthy and difficult to understand. Creditors, on the other hand, have encountered increasing difficulty in keeping current with a steady stream of administrative interpretations and amendments, as well as highly technical judicial decisions. There is also evidence that many creditors have sincerely tried to comply with the act but, due to its increasing complexity and frequent changes, have nonetheless found themselves in violation and subject to litigation. In addition, this committee and other congressional and government sources have found the level of administrative enforcement by the Federal bank agencies seriously inadequate. In short, the committee believes that the interests of both consumers and creditors would be furthered by simplification and reform of the act."

With particular reference to the amendment of the disclosure requirements of § 1638(a), the Senate Report says, Id. p. 864:

"The security interest disclosure is also simplified to eliminate the technical disclosure of the type of security interest taken. When a security interest is being taken in property purchased as part of the credit transaction, this section requires a statement that a security interest has been or will be taken in the property purchased. When a security interest is being taken in property not purchased as part of the credit transaction, *the Committee intends this provision to require a listing by item or type of the property securing the transaction, but not a listing of related or incidental interests in the property.* For example, a loan secured by an automobile (not being purchased with the proceeds of the loan) would require a statement indicating that the loan is secured by an automobile but would not require a listing of incidental or related rights which the creditor may have such as insurance proceeds or unearned insurance premiums, rights arising

under, or waived in accord with state law, accessions, accessories or proceeds." (Emphasis supplied)

S. Rep. No. 96-73 says, Id. at 879-880:

> "The subcommittee learned that judging from consumer tests in other areas, the typical disclosure statement utilized today by creditors is not an effective communication device. Most disclosure statements are lengthy, written in legalistic fine print, and have essential truth in lending disclosures scattered among various contactual [sic] terms.
>
> The result is a piece of paper which appears to be 'just another legal document' instead of the simple, concise disclosure form Congress intended."

Ford Motor Credit Co. v. Milhollin, —— U.S. ——, 48 L.W. 4145, decided February 20, 1980, was concerned with the imposition of the statutory liability under TILA for a claimed nondisclosure of an acceleration clause. The Court concluded, 48 L.W. at 4146, that the issue of acceleration disclosure "is not governed by clear expression in the statute or regulation, and • • • it is appropriate to defer to the Federal Reserve Board and staff in determining what resolution of that issue is implied by the truth in lending enactments." The Court examined the Federal Reserve Board staff treatment of acceleration disclosure and denied imposition of the statutory liability.

We are aware of no administrative interpretations pertinent to the particular issue before us. Public Position Letter No. 377, quoted in Edmondson, 577 F.2d 295, n. 8, relates to life insurance, not physical damage insurance. Staff Letter 1263, Consumer Credit Guide (CCH) ¶ 31,736 (November 23, 1977), an unofficial interpretation, leaves to state law the question of whether a security interest has been acquired by the creditor and, if so, whether that interest has been adequately identified.

In Milhollin, supra, 48 L.W. at 4149, the Court said:

> "The concept of 'meaningful disclosure' that animates TILA (citation omitted), cannot be applied in the abstract. *Meaningful* disclosure does not mean *more* disclosure. Rather, it describes a balance between 'competing considerations of complete disclosure . . . and the need to avoid . . . informational overload' (citations omitted) and striking the appropriate balance is an empirical process that entails investigation into consumer psychology and that presupposes broad experience with credit practices." (Emphasis in original).

The Milhollin approach parallels the intent of Congress in enacting the 1980 amendments and the legislative history of those amendments. The effort is to strengthen the impact of TILA by simple, concise disclosures which can be understood by consumers and creditors. The installment contract in issue identifies the security interest taken in the property purchased, the pick-up truck. The insurance charge is specifically noted on the face of the contract and is included in the total amount which must be repaid in monthly installments. The insurance on damage to the vehicle was part of the credit transaction. The right of the seller to the returned premium would seem to be part of the "proceeds" of that transaction. If not such a part, the returned premium is property not purchased. The Senate Report, supra p. 864, says with reference to property not purchased, that the disclosure need not include "a listing of incidental or related rights which the creditor may have such as insurance proceeds or unearned insurance premiums." We are convinced that the Act does not require, and Congress did not intend it to require, an exemplification of that interest on the face of the installment contract. Because of this conclusion, we need not delve into the legal complexities of the Third Circuit decision in Gennuso, 566 F.2d 437; the Fifth

Circuit decision in Edmondson, 577 F.2d 291; and the Seventh Circuit decision in Valencia, —— F.2d ——.

The application of Milhollin and the 1980 actions of Congress present no retroactivity problem. We are concerned only with civil liability for nondisclosure. The buyers have shown no damage. Our decision establishes no new principle of law. Rather, it recognizes the congressional intent. Application to this case furthers the operation of TILA and produces an equitable result. See Chevron Oil Co. v. Huson, 404 U.S. 97, 106-107.

Affirmed.

No. 78-1806—JAMES v. FORD MOTOR CREDIT COMPANY, et al.

DOYLE, Circuit Judge, dissenting.

Because of my belief that the seller's right to unearned and returned premiums is a security interest, and thus the installment purchase contract here violates the Truth in Lending Act, I respectfully dissent.

The question is whether the provision in the contract which provides that the buyer assigns to the seller any monies payable under the insurance (on the car), including returned or unearned premiums, and which authorizes the seller on behalf of both parties to receive or collect same constitutes a violation of the Truth in Lending Act.

Regulation Z, 12 C.F.R. Section 226.2(gg), defines security interest as meaning "any interest in property which secures payment or performance of an obligation. The terms include, but are not limited to, security interests under the Uniform Commercial Code. . . ."

This problem is not a new one. Three circuits have considered this issue and have held that the nondisclosure of

the seller's right to unearned and returned premiums violates the Truth in Lending Act and subjects the seller to the remedy which is being pursued here. The cases are Gennuso v. Commercial Bank & Trust Company, 566 F.2d 437 (3rd Cir. 1977); Edmondson v. Allen-Russell Ford, Inc., 577 F.2d 291 (5th Cir. 1978), *cert. denied* 441 U.S. 951; and Valencia v. Anderson Brothers Ford, —— F.2d —— (7th Cir. March 20, 1980).

The earliest of these decisions is Gennuso v. Commercial Bank & Trust Co., *supra*. Here the plaintiff charged that the Commercial Bank and Trust Company failed to properly identify in the Disclosure Statement and in the Note and Security Agreement a security interest in the proceeds and the unearned premiums in a property insurance policy covering the automobile that he had purchased. It was alleged that such failure violated the Truth in Lending Act and Regulation Z. No mention of the security interest in the insurance policy was made at the top of the note where the collateral was described. There had been some slight mention of the interest in question in the note and security agreement. It was held that the use of general language in this document was sufficient. It was said that the mention of the security interest in after-acquired property satisfied the requirements of the Act. The court held that the conduct of the bank constituted a violation of the Truth in Lending Act and Regulation Z as well.

To the same effect is Edmondson v. Allen-Russell Ford, Inc., *supra*. Here again the court held that the assignment of a returned or unearned premium of an insurance policy was a security interest for purposes of Regulation Z, in accordance with the Truth in Lending Act, and had to be disclosed. The court, through Goldberg, J., had no difficulty concluding that the unearned portion of the premium was a security interest which had to be disclosed. The court relied on Gennuso v. Commercial Bank & Trust Co., *supra*.

Here again the court ruled that it was inadequate to construe the general provision that the " 'Seller shall have a security interest under the Uniform Commercial Code in the Property (described above) and in the proceeds thereof. . . .' " 577 F.2d at 295. The court said that the "lender must disclose the type of security interest held, retained, or acquired and the property of the borrower which serves or will serve as the collateral." 577 F.2d at 295. A sufficient description was determined to be essential.

The third of the recent circuit cases is Valencia v. Anderson Brothers Ford, *supra,* from the Seventh Circuit. The court said:

> We therefore affirm the district court's ruling that an assignment of unearned or returned insurance premiums in a consumer credit installment contract is a security interest for purposes of disclosure under the TILA. This result is consistent with the liberal interpretation to be given the Act, the majority of federal court decisions addressing the issue, and a Federal Reserve Board staff interpretation of a closely analogous issue. In view of the interest in uniformity in TILA disclosures and in the absence of any persuasive argument to the contrary, we decline to break with the Third and Fifth Circuits on this issue.

Slip op. at p. 14.

The majority was influenced by the fact that on March 31, 1980, the President approved the "Truth in Lending Simplification and Reform Act," which amended 15 U.S.C. Section 1638(a), the disclosure section of the Truth in Lending Act. As amended, it was pointed out by the majority that this section permits disclosure of the principal property which provides the security for the loan. It does not require, so the Report says, a listing of related or incidental interests in the property, and it gives as an example a loan secured by an automobile which is not being purchased with the proceeds of the loan, but which would require a state-

ment indicating that the loan is secured by an automobile. It would not require a listing of incidental or related rights which the creditor may have such as insurance proceeds or unearned insurance premiums.

The majority also calls attention to the recent opinion of the Supreme Court in Ford Motor Credit Co. v. Milhollin, —— U.S. ——, 48 L.W. 4145, decided February 20, 1980, which adopted the approach that security documents have, in the past, carried too much excess luggage and that they should disclose with simplicity and should limit themselves to the disclosure of the matters having to do with the security itself. This may well be the present tendency, but at the time of the occurrence in question the approach which is shown by the Third, Fifth and Seventh Circuits obtained.

In summary, the automobile insurance policy and, of course, the premium which is paid to obtain the coverage, are part and parcel of the entire automobile financing business. It makes the loan more secure.[1] Thus the unearned premium which would ordinarily go to the insured and which is being held back by the lender is information of genuine interest to the purchaser-insured, and it is not possible to cause it to be unimportant.

The new approach might render the procedure less complicated. Nevertheless, I submit that we are not justified in adopting this concept so as to apply it to the present set of facts and to do so only on the basis of legislative history which attended the enactment of the amendments. Even if the legislative history would call for a different result, it should not be applied here in a retroactive way.

For the reasons stated, I disagree with the majority opinion.

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[1] If, for example, the automobile were to be stolen or totaled out in an accident, there would be no security in the absence of insurance.

ORDER OF THE COURT OF APPEALS
DENYING PETITION FOR REHEARING
(July 21, 1980)

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

JODY JAMES and BARBARA JAMES, Plaintiffs-Appellants,	)	
v.	)	No. 78-1806
FORD MOTOR CREDIT COMPANY and DEL NORTE MOTOR COMPANY, Defendants-Appellees.	)	

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLORADO
(D. C. No. Civ. 78-F-647)

Before SETH, Chief Judge, BREITENSTEIN, HOLLOWAY, McWILLIAMS, BARRETT, DOYLE, McKAY, LOGAN and SEYMOUR, Circuit Judges.

PER CURIAM.

ON PETITION FOR REHEARING

The petition for rehearing is denied. The petitioners-appellants object to the consideration which the court gave to the

March 31, 1980, "Trust [sic] in Lending Simplification Act" and its legislative history. The Supreme Court has said that when two acts are in *pari materia*, the later act can be "regarded as a legislative interpretation of the earlier." *United States v. Stewart*, 311 U.S. 60, 64. In *Regents of the University of California v. Bakke*, 438 U.S. 265, 349, the separate opinion of four Justices says: "We have repeatedly recognized that subsequent legislation reflecting an interpretation of an earlier Act is entitled to great weight in determining the meaning of the earlier statute."

The 1968 and 1980 acts related to the same subject matter. "Truth in Lending." We are convinced that the 1980 Act reflects an interpreation [sic] by Congress of the earlier act and is entitled to great weight. The effect is that Congress in passing the 1968 act did not intend to impose a civil penalty for the type of nondisclosure claimed by the appellants.

Judge Doyle would grant the petition for rehearing.

The petition for rehearing having been denied by the panel to whom the case was argued and submitted and no member of the panel nor judge in regular active service on the court having requested that the court be polled on rehearing en banc. Rule 35, Federal Rules of Appellate Procedure, the suggestion for rehearing en banc is denied.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

JAMES SHANKS, Plaintiff, vs. GREENBRIAR DODGE, INC., Defendant.	CIVIL ACTION NO. C75-1154A

MAGISTRATE'S REPORT AND RECOMMENDATION

On April 10, 1975, James Shanks purchased an automobile from Greenbriar Dodge. He financed the transaction by entering into a consumer credit agreement with the defendant, who was a creditor within the meaning of the Consumer Creditor Protection Act, 15 U.S.C. § 1601, *et. seq.* Shanks is a natural person who borrowed the money from the defendant primarily for household and family purposes.

On June 17, 1975, Shanks, through counsel, filed a complaint charging that the defendant's contract for credit was violative of the Truth-in-Lending law, in that not all required disclosures were made thereon.

On August 24, 1976, the Honorable Ezra H. Cohen filed his recommendations as to the initial contentions. On September 10, 1976, and before the Report and Recommendation had been ruled upon by the District Court, the plaintiff filed a supplemental memorandum in support of his motion for summary judgment, raising an additional ground which is the subject of this Report and Recommendation.

In his supplemental memorandum, the plaintiff contends that the defendant retained a security interest in any un-

earned premiums paid on the insurance on the collateral. This retained right is not shown on the disclosure statement in the section which purports to list all security interests retained.

The only security interest set out in the disclosure statement is as follows:

> 13. Security Interest: Seller shall have a Security Interest, as the term is defined in the Uniform Commercial Code of the state in which this contract is executed, in the property until all amounts due under this contract are paid in full.

Item 6 of the "undisclosed" section of the "Additional Terms and Conditions" of the Security Agreement provides in part as follows:

> 6. Buyer agrees to keep the property insured at buyer's expense against substantial risks of damage, destruction, or loss for so long as any amount remains unpaid on this contract with loss payable to the seller as its interest may appear . . . the proceeds from vehicle insurance, by whomever procured, shall be applied toward replacement of the property or payment of the obligation hereunder, in the sole discretion of seller. Buyer hereby assigns to seller any monies not in excess of the unpaid balance due under this contract, that may become payable under such insurance, by whomever obtained, including return of unearned premiums and authorizes and requests any insurance company to make payment of such monies directly to seller to be applied to the unpaid balance hereunder, and buyer appoints seller as buyer's attorney-in-fact to endorse buyer's name upon check or draft representing payment to buyer of such monies.

This identical contention is made in a good number of cases presently under submission to the Magistrate. A vir-

tually identical situation has previously been submitted to the District Court in *Edmondson* v. *Allen-Russell Ford, Inc., et al.*, Civil Action No. 75-940A (N.D.Ga. 1976). In this Report and Recommendation, Judge Cohen noted in passing that he felt that the situation set out above created a security interest which ought to be disclosed. The Report and Recommendation was adopted by the Honorable Newell Edenfield as no objection was made. Apparently, Judge Cohen did not consider that case as a final disposition of the issue, for in the case *sub judice,* he issued a *WITHDRAWAL OF RECOMMENDATION* filed October 27, 1976, in which he noted that:

> Since the defendant in *Edmondson* admitted that the clause created a security interest, *Edmondson* may be distinguished from this case where there is no such admission.

From a review of the cases submitted to this Magistrate recently, it would appear that under these circumstances, most lenders in the District claim the same right in the unearned premiums which the defendant here did, and it would appear further that this fact is not disclosed as a security interest. Because of the import of the issue, a detailed analysis is in order.

Congressional intent in the legislation seems an apt point of beginning. Credit for the whole notion is given to Senator Paul H. Douglas of Illinois who first suggested the need for such a bill seven years prior to its passage in 1968. It was the Senate who first passed a Truth-in-Lending bill in 1967. That bill was passed in lieu of the House bill after substituting for its language much of the text of the House bill. The House report of the Committee on Banking and Currency said of the Truth-in-Lending portion that:

> It provides for full disclosure of credit charges, rather than regulation of the terms and conditions under

> which credit may be extended. It is the view of your committee that such full disclosure would aid the consumer in deciding for himself the reasonableness of the credit charges imposed and further permit the consumer to "comparison shop" for credit. 1968 *U.S.C. Cong and Admin News* 1963.

The Committee noted that, in speaking for the legislation, President Johnson said in part:

> The Consumer has the right to know the cost of this key item of his budget just as much as the price of any other commodity he buys. If consumers are to plan prudently, and to shop wisely for credit, they must know what it really costs. In many instances today consumers do not know the cost of credit. Charges are often stated in confusing or misleading terms. They are complicated by "add ons" and discounts and unfamiliar gimmicks. The Consumer should not have to be an actuary or a mathematician to understand the rate of interest that is being charged. As a matter of fair play to the consumer, the cost of credit should be disclosed fully and simply. *Id.* at 1965.

In listing then existing disclosure practices which the Committee condemned, it dealt only with those practices which obscured the rate of charge and the dollar cost of credit. *Id.* at 1970. In a close perusal of the House report, nowhere has this Magistrate been able to see one indicia of concern for whether or not security interests were disclosed. The Conference Committee's report does not deal with whether or not any security interest ought to be disclosed. The Conference Committee's report does, however, discuss the disclosures about which the Congress was concerned with reference to property and liability insurance. It is apparent that the conferees considered the cost of premiums for property and liability insurance to be the only item which ought to be disclosed. By compromise they reached the conclusion that under the facts of this transac-

tion, not even their cost must be itemized, disclosed, or included in the finance charge. *Id.* at 2022.[1]

Although the Act, as finally passed, and Regulation Z, as promulgated by the Federal Reserve Board, require the disclosure of retained security interest generally, it seems clear that both enacting bodies gave considerable attention to the issue of how to disclose matters pertaining to insurance purchased incident to the acquisition of credit, and neither has specifically required the disclosure which the plaintiff contends ought to have been made.

On July 22, 1970, an opinion letter issued from the Board saying that where a single premium *lifetime* accidental death and dismemberment policy was purchased out of the proceeds of the loan and where the creditor was designated as owner of the policy during the term of the loan, it would be appropriate to disclose the loan company's ownership of the policy as a type of security interest.[2]

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[1] The Conference substitute did not require disclosure of such insurance premiums if the debtor is clearly informed of his right to choose where to buy such insurance.

[2] As we understand the proposed plan, your client proposes to place literature in its loan offices concerning insurance to be sold by a company unrelated to your client. Applications for single premium lifetime accidental death and dismemberment policies are available in each office and if a customer desires to purchase such a policy with the proceeds of his loan, a check will be sent directly to the Company from your client in payment of the premium. While your client will not require the purchase of this insurance and the proceeds of the policy would in no circumstances be used to pay any portion of an unpaid balance of the loan, your client would be designated as owner of the policy during the term of the loan. In the event of the customer's default, your client would have the right to cancel the policy and apply any premium refund to the unpaid balance of the loan.

Under the circumstances, we think it would be appropriate to disclose the loan company's ownership of the policy as a type of

This Court would not read that opinion letter to make the disclosure obligatory. The use of the word "appropriate" makes the letter seem advisory in nature rather than imperative when viewed against the usual language in Board opinion letters which are noteworthy for positively setting out the agency's opinion in absolute terms.[3]

Even if the opinion letter were accorded full deference, it is not controlling of the situation here. In the hypothetical to which the Board addressed itself, the borrower purchased something of independent value whose existence was not tied to the term of the loan. It is analogous to the situation where a car purchaser also buys a boat trailer from the dealer and finances both with the loan. Clearly in that instance if the small print gives the creditor a security interest in both, that ought to be disclosed. In the hypothetical, the insurance is not taken out solely to protect the value of the collateral or the repayment ability of the borrower during the period of the loan, as is the case at hand.

The argument is made that the right of the creditor to unearned property insurance premium is not a security in-

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"security interest" under Section 226.8(b)(5), and disclosures need not be made under Section 226.4(a)(5). The amount of the premium would not be included in the "finance charge" nor would it be disclosed as an "other charge".

Tynan Smith, Assistant Director

[3] It is understood that Federal Reserve Board staff opinion letters are, "entitled to great weight" for they constitute part of the body of "informed, experience and judgment of the agency to whom Congress delegated appropriate authority." *Philbeck* v. *Timmers Chevrolet, Inc.*, 499 F.2d 971, 976 (5th Cir. 1974). But, such letters are not rules, regulations or interpretations within the meaning of 18 U.S.C. § 1640(f). See *Jones* v. *Community Loan and Investment Corp.*, slip opinion page 248, December 13, 1976 (5th Cir.); *Ives* vs. *W. T. Grant Co.*, 522 F.2d 749, 758 (2nd Cir. 1975).

terest at all. Some would contend that it is not a security instrument under the Uniform Commercial Code, and others contend that it is not a security interest under the Truth-in-Lending Act and its regulations which perhaps encompass more situations than does the Uniform Commercial Code. It is pointed out that the language of the contract gives an outright assignment of monies due the borrower from an insurance company to the lender.

The definition of "security interest" in the Uniform Commercial Code [*Ga. Code Ann.* § 109 A-1-201(37)] is in pertinent part:

> "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation.

Thus, a creditor's right to the property is conditioned on the status of the underlying debt.

On the other hand, "assignment" is defined, generally, as:

> A transfer or making over to another of the whole of any property, real or personal, in possession or in action, or of any estate or right therein. *Black's Law Dictionary,* Fourth Edition, 1951.

Under the conditions of the loan agreement in the case at bar, if an insurance company cancelled a policy or refused to accept the risk, which it might do for a variety of reasons, this would result in returned premiums; yet, the debt contract would still be in place so long as the debtor honored the contract by payment in accordance with its terms. Unlike the situation with a bona fide security interest, the defendant in this case has an absolute right to the returned premiums even if the debt is not in default. It is supposed that for that reason one of the commentators has noticed that:

> The following are not security interest [sic] within the definition of the Code . . . (b) an absolute assignment. An absolute assignment of money due under a contract in payment of a debt owed by the assignor is not the creation of a security interest under the Code. . . . 1 *Anderson, Uniform Commercial Code,* § 1-201:110, 2nd Edition, 1970.

It is also interesting to note that in Georgia a transfer of an interest or claim in or under any policy of insurance is not treated as a secured transaction. *Ga. Code Ann.* § 109A-9-104(f).

The fact that the "assignment" in this case may not be a security interest within the meaning of the Uniform Commercial Code, however, is not finally determinative. In Regulation Z "security interest" and "security" are defined to mean:

> Any interest in property which secures payment or performance of an obligation. The terms include, but are not limited to, security interest under the Uniform Commercial Code, real property mortgages, deeds of trust, and other consensual and confessed liens whether or not recorded, mechanics, materialmen, artisans, and other similar liens, vendors liens in both real and personal property, the interest of the seller in a contract for sale of real property, any lien on property arising by operation of law, and any interest in a lease when used to secure payment or performance of an obligation. 12 C.F.R. 226.2(gg).

Even under the definition contained in Regulation Z, it is not clear that the assignment in question is a security interest. The creditor has two separate considerations in this loan. The first is to obtain a security interest in the automobile which is being used as collateral. Second, he has an interest in seeing that his collateral does not become worthless because of loss, damage, or destruction. To protect the collateral, the loan agreement in a separate section requires the borrower to obtain property insurance but

ultimately gives to the lender the full power to keep the property protected, and it gives to him the right to be recompensated if ultimately he must act to protect the value of the collateral. It follows then that if the lender must act to provide the protection of collateral, he ought to be able to take advantage of such monies as have been expended by the borrower to provide this protection.

This Court is saying then that it views the assignment as giving the borrower a right to monies to be used for the protection of the collateral and that the contract rights so obtained did not come into existence primarily to create additional security for the credit. Therefore, this right of the creditor is not seen as a security interest within the meaning of that term as defined in Regulation Z and, therefore, no disclosure is required.

The Fifth Circuit recently has had an occasion to examine a credit contract much like the one here. In that case the borrower complained that the disclosure was inadequate because it did not mention the creditor's right of repossession of the collateral. In denying relief on that point, the Court noted that neither the Act nor the regulations imposed upon the creditor the obligation to set forth a list of its rights as a secured party. *Grant* v. *Imperial Motors,* 539 F.2d 506, 509 (5th Cir. 1976).

While others may posit a decision on this issue turning on whether or not this assignment is a security interest, this Magistrate is impressed with the rationale applied in the Third and Fifth Circuits in a number of recent cases dealing with acceleration causes [sic] which, it is felt, is the denouement of the instant issue also.

The birth of the rationale is ascribed by the Fifth Circuit to the case of *Johnson* v. *McCrackin-Sturman Ford, Inc.,* 527 F.2d 257 (3rd Cir. 1975). In that case the plaintiff contended and the Court below held that payments made

due by the exercise of the acceleration clause were "charges" within the meaning of the phrase, "default, delinquency, or similar charges payable in the event of late payments", which must be disclosed according to Section 226.8(b)(4) of Regulation Z. In finding to the contrary, the Court of Appeals noted that "disclosure" was a term of art under the Truth-in-Lending Act which was intended by the Congress to give the consumer a list of credit items considered important by the Congress so that he might be well equipped to choose the credit contract that best fit his needs. The Court went on to note that probably there was no installment contract in force today that did not contain a clause granting the creditor the right to require immediate payments of all installments upon the happening of a specified event. The decision assumed that the Congress intended to deal with commercial realities and found that charges of the type referred to in the Regulation meant additional amounts due beyond the disclosed indebtedness. In concluding, the Third Circuit said:

> However, no matter how desirable we might think it to underscore a creditor's right to accelerate payment upon default, the question to which we are, of course, limited is whether the specific provisions of the Truth-in-Lending Act or Regulation Z require including of this right in the disclosure statement. *Id.* at 269.

Essentially the same issue was presented to the Fifth Circuit in a trilogy of cases before a panel of Wisdom and Morgan, Circuit Judges, and Lynne, District Judge.[4] That

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[4] *Martin* vs. *Commercial Security Company, Inc.*, 539 F.2d 521 (5th Cir. 1976), *Myers* vs. *Clearwater Dodge Sales, Inc.*, 539 F.2d 511 (5th Cir. 1976), *Grant* vs. *Imperial Motors*, 539 F.2d 506 (5th Cir. 1976). But the per curiam opinion in *McDaniel* vs. *Fulton National Bank*, slip opinion page 171, December 6, 1976 (5th Cir.), decided by a different panel, seems to invite a petition for rehearing *en banc*.

panel reached the same conclusion reached in the Third Circuit and cited that Circuit's decision liberally with approval.

The key case is *Martin*. Judge Lynne, writing for a unanimous panel, began by noting that:

> The Congressional finding that "the informed use of credit results from an awareness of the cost thereof by consumers" is the principal theme of the Act. Consequently, the Act and the Regulations promulgated thereunder require the full disclosure *of certain credit terms* which Congress and the Federal Reserve Board have deemed essential to "informed use of credit". *Id.* at 523. (Emphasis added)

A page later the opinion continues in the same vein:

> While (the Act) and (the Regulations) enumerate the credit terms to be disclosed in consumer credit sales not under an open end credit plan, neither section specifically requires disclosure of the creditor's right to accelerate payment upon default, nor is there any official Board interpretation requiring such disclosure. It is highly illuminating that there is no reference in the Act, the Regulations, or the official interpretations of the Federal Reserve Board, to acceleration clauses or the right to accelerate payments, even though Congress has set forth in the Truth-in-Lending Act those credit terms it considers essential to the informed use of credit and has mandated uniformity in terminology and manner of presentment in order to assure a meaningful disclosure of such terms. It is the task of the Board armed with delegated authority, to implement the policy of the Act and not that of the Court.

The opinion concludes as follows:

> We hold that in the absence of the Regulation requiring it, failure to disclose an acceleration clause and the lender's rebate policy with respect thereto in an installment credit transaction does not give rise to a claim for statutory damages. *Id.* at 529.

The rationale then is that disclosure, as used in the Truth-in-Lending Act, means the meaningful disclosure of the specific terms set out by the Congress, and the lawful regulations and opinions of the Federal Reserve Board. It is conceded that these generally require the disclosure of security agreements. Here that is of no consequence for the Congress and the Board have given considerable study to the cost of insurance incident to the obtaining of credit and have specifically set out those disclosures which it was felt effectuated the policy of the Act. As both bodies have thoroughly considered the insurance premium issue and have not required the disclosure sought here, then this Court should not.

REPORTED AND RECOMMENDED this 10th day of December, 1976.

/s/ J. OWEN FORRESTER

J. Owen Forrester
United States Magistrate

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

JAMES SHANKS, *Plaintiff*, vs. GREENBRIAR DODGE, INC., *Defendant*.	CIVIL ACTION NO. C75-1154A

ORDER

After having carefully reviewed the Magistrate's Report and Recommendation in this case, it is received with approval.

Let a copy of this Report and Recommendation and Order be served upon counsel for the parties.

If no objection is made within ten (10) days of this Order the Magistrate's Report and Recommendation will be adopted as a record of the proceedings below and as the opinion and Order of the Court.

SO ORDERED this 16th day of December, 1976.

CHARLES A. MOYE, JR.
Charles A. Moye, Jr.
United States District Judge

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 78-2562

GLENN A. SOUIFE,

Plaintiff-Appellant,

vs.

FIRST NATIONAL BANK OF COMMERCE,

Defendant-Appellee.

Appeal from the United States District Court
for the Eastern District of Louisiana

ON PETITION FOR REHEARING EN BANC

(December 5, 1980)

Before THORNBERRY, ANDERSON, AND THOMAS A. CLARK,

Circuit Judges.

PER CURIAM:

The court will defer further consideration of the petition for rehearing en banc pending decision by the Supreme Court in *Anderson Bros. Ford* v. *Valencia,* 617 F.2d 1278 (7th Cir.), *cert. granted,* 48 L.W. 2654 (November 11, 1980) (No. 80-84).

ENTERED FOR THE COURT:

/s/ R. Lanier Anderson, III
United States Circuit Judge

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Reg. Z; FC-0173]

TRUTH IN LENDING

Proposed Official Staff Interpretation

AGENCY:

Board of Governors of the Federal Reserve System.

ACTION:

Proposed official staff interpretation.

SUMMARY:

In accordance with 12 CFR 226.1(d)(2), the Board staff is publishing for comment official staff interpretation FC-0173 of Regulation Z, Truth in Lending, regarding security interest disclosures in closed end credit transactions. The proposed interpretation holds that a creditor need not disclose as a security interest its right to receive insurance proceeds or unearned premiums nor does it need to disclose that it is named as loss payee or beneficiary on an insurance policy.

DATES:

Comments must be received on or before October 20, 1980.

ADDRESS:

Comments (including reference to FC-0173) may be mailed to Secretary, Board of Governors of the Federal Reserve System, Washington, D.C. 20551, or delivered to Room B-2223, 20th and Constitution Avenue, N.W., Wash-

ington, D.C. between 8:45 a.m. and 5:15 p.m. Comments may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m.

FOR FURTHER INFORMATION CONTACT:

Claudia J. Yarus, Staff Attorney, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, Washington, D.C. 20551 (202-452-3667).

SUPPLEMENTARY INFORMATION:

(1) The text of official staff interpretation FC-0173 is published with identifying details deleted to the extent required to prevent a clearly unwarranted invasion of personal privacy. The Board maintains and makes available for public inspection and copying a current index providing identifying information for the public, subject to certain limitations stated in 12 CFR Part 261.6.

(2) The letter is being issued as a proposal, rather than in final form, and interested persons are invited to submit relevant comment.

(3) After comments are considered, this official staff interpretation may be amended, may be withdrawn or may remain unchanged. Final action regarding this official staff interpretation will appear in the *Federal Register*.

(4) Authority: 15 U.S.C. 1640(f).

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§ 226.2(gg) Creditor is not required to disclose as a security interest its right to receive insurance proceeds or unearned insurance premiums nor to disclose that it is named as loss payee or beneficiary on an insurance policy.

§ 226.8(b)(5) " " "

This is in response to your letter requesting an official staff interpretation regarding security interest disclosures under § 226.8(b)(5) of Regulation Z. You wish to know

whether the creditor's right to receive proceeds or unearned premiums from a property or a credit life insurance policy must be disclosed as a security interest. You also ask if a security interest should be disclosed where a creditor requires that it be named as the loss payee on a property insurance policy or as the beneficiary on a credit insurance policy.

Section 226.8(b)(5) addresses disclosure of security interests in other than open end credit transactions. It requires disclosure of the type of security interest taken and identification of the property to which that interest relates.

The staff believes that a creditor is not required by this section to disclose its right to receive insurance proceeds or unearned insurance premiums nor to disclose that it is named as loss payee or beneficiary on an insurance policy. Truth in Lending disclosures are meant to provide useful information to consumers to enhance credit shopping. Consumers do need to know that they risk the loss of certain property if they default. The disclosures under § 226.8(b)(5) inform consumers of which property is subject to that risk at the time the credit decision is being made. We believe that information regarding the creditor's interest in insurance proceeds and unearned premiums would not be used in comparison shopping. Although a technical reading of the security interest definition might cover a creditor's interest in insurance proceeds and unearned premiums, it is our opinion that such incidental interests are not the type of interests meant to be covered by § 226.8(b)(5).

The staff recognizes that there are a number of circuit court decisions to the contrary. We believe, however, that our position better serves the purpose of the statute and the regulation to convey in a meaningful way information that can be used by consumers in shopping for credit.

This is an official staff interpretation of Regulation Z, issued in accordance with § 226.1(d)(2). It is limited to the facts and issues discussed herein.

Sincerely,

JANET HART
Director

Board of Governors of the Federal Reserve System, September 18, 1980.

(signed) THEODORE E. ALLISON
Theodore E. Allison
Secretary of the Board

[SEAL]

FEDERAL RESERVE SYSTEM

12 CFR Part 226

[Reg. Z; FC-0173]

TRUTH IN LENDING

Proposed Official Staff Interpretation; Deferral of Final Action

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Deferral of final action.

SUMMARY: By notice published on September 24, 1980 (45 FR 63295), the Board staff requested comment on proposed Official Staff Interpretation FC-0173 of Regulation Z, Truth in Lending, regarding security interest disclosures in closed end credit transactions. The comment period ended on October 24, 1980. In light of the Supreme Court's grant of certiorari in *Anderson Bros. Ford* v. *Valencia, cert. granted,* 49 USLW 3350 (1980) (No. 80-84, 1980 Term), the staff believes it is inappropriate to take final action on the interpretation at this time.

FOR FURTHER INFORMATION CONTACT:

Claudia J. Yarus, Staff Attorney,
Division of Consumer and Community Affairs,
Board of Governors of the Federal Reserve System,
Washington, D.C. 20551 (202-452-3667).

Board of Governors of the Federal Reserve System, December 15, 1980.

Theodore E. Allison,
Secretary of the Board.